

U.S. SANCTIONS ON IRAN: NEXT STEPS

Y 4. IN 8/16: IR 1

U.S. Sanctions on Iran: Next Steps, ... JG

BEFORE THE
SUBCOMMITTEE ON
INTERNATIONAL ECONOMIC POLICY AND TRADE
OF THE
COMMITTEE ON
INTERNATIONAL RELATIONS
HOUSE OF REPRESENTATIVES
ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

MAY 2, 1995

Printed for the use of the Committee on International Relations



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U.S. SANCTIONS ON IRAN: NEXT STEPS

TUESDAY, MAY 2, 1995

HOUSE OF REPRESENTATIVES,
COMMITTEE ON INTERNATIONAL RELATIONS,
SUBCOMMITTEE ON INTERNATIONAL
ECONOMIC POLICY AND TRADE,
Washington, DC.

The subcommittee met, pursuant to call, at 2:05 p.m. in room 2128, Rayburn House Office Building, Hon. Toby Roth (chairman of the subcommittee) presiding.

Mr. ROTH. This hearing is scheduled for 2 o'clock, so we will begin. We have a vote on the floor, so we will have some more members coming in later.

Let me say this is a very important hearing today because we feel that by imposing an embargo on Iran, the President has now fired the biggest economic weapon in our arsenal. In today's hearing we will consider the overriding question: "Will an embargo against Iran work for us or against us?"

I am concerned that in firing this economic weapon we won't hit Iran but will end up shooting ourselves in the foot. We have to ask ourselves: "Will this embargo actually hurt Iran or will the real casualties be U.S. exporters and American workers injured by friendly fire from our own government?"

Yesterday the White House admitted that this embargo will cost thousands of American jobs. Moreover, Iran owes \$400 million to U.S. companies. What chance is there that Iran will pay these bills now, or will these U.S. companies simply be the first to feel the impact of the embargo?

An embargo is all about leverage, imposing economic pain to force Iran to drop its nuclear weapon program and stop its terrorism and subversion.

Without question, Iran is a rogue regime. But if the threat from Iran is so great, then we need a policy that works, not just another futile gesture.

The United States cannot succeed if we go it alone against Iran. For 16 years the United States has maintained a lonely vigil against Iran, with no results. Look at the facts. In 1993, Iran's total trade was some \$29 billion. U.S. exports to Iran were only \$616 million, barely a few percent of the total. What is more, Iran's total GNP is some \$300 billion. So the question is, "where is our leverage?"

Now, if other countries joined this embargo, we would have a bigger stick. But the United States is still all alone. Iran's biggest trading partners are among our closest allies, but none of them has

shown the slightest willingness to follow our lead: not Japan, not Germany, not Italy, not France, not South Korea—and these are Iran's five major top trading partners. Their total trade with Iran is some \$13 billion, and they are all trying to increase their trade with Iran, not cut it back.

Some in Congress are proposing a boycott on any foreign company that trades with Iran. But if our allies are going in the other direction, would a boycott isolate Iran or would it isolate the United States?

Without international cooperation, it is hard to see how a U.S. embargo is anything more than a futile gesture. In short, if the U.S. policy makes the United States weaker—not Iran—then what will we have accomplished in this endeavor?

To deal with these questions we have some of the best experts on Iran, on the use of sanctions, and on the impact of the embargo on U.S. companies. That is why we are having this hearing today at this very crucial time. I am looking forward to the expert testimony that we are going to receive today.

Our first witness is going to be Representative Peter King. We welcome our colleague, Mr. King, of New York. Representative King has introduced H.R. 1033, which would impose an economic embargo against Iran. The bill also would forbid American citizens from engaging in any transactions with Iranian nationals anywhere in the world.

But before we ask Congressman King for his testimony, let me turn to the ranking member of our committee, Mr. Gejdenson, and congratulate him on his recent victory.

Mr. GEJDENSON. Thank you, Mr. Chairman.

As always, it is a pleasure working with you. I would like to commend you for holding this hearing and for addressing this very serious issue. I think a thoughtful and constructive debate on the decision by the administration is important.

On Sunday, the President of the United States took a bold and decisive step by imposing a total embargo on Iran. It left no room for interpretation. The United States considers Iran to be an outlaw and is simply unwilling to make believe that Iran is among the family of civilized nations.

The President of the United States has done the right thing. He has done the smart thing. Oftentimes during the cold war, the United States had to stand alone at the beginning of a challenge to those who oppressed human rights and freedom. Whether in confronting the Soviet Union or racism in South Africa, there were many times that American principles had to lead the world, and it is clear that American principles and courage will have to lead the world here again today.

There seems to be very little in the way of disagreement as to U.S. objectives in regard to Iran. Iran needs to end its support for terrorism, much of which is designed to undermine the Middle East peace process. Iran must cease its development of weapons of mass destruction and missiles by which to deliver them. Iran must significantly alter its abhorrent record on human rights.

The U.S. action in the Gulf war significantly reduced any threat to Iran. The burden is now on our allies to come along with us. Thus far, the strategy of a constructive dialogue embraced by many

of our allies has, to be put delicately, been less than successful. To put it bluntly, Iran has paid no attention and paid no price for its support and financing of international terrorism around the globe.

There are countries, even those with which we have significant differences, where a constructive dialogue could serve to further our objectives. Iran is clearly not among those nations. It is a rogue regime that is intent upon fomenting unrest in the region and determined to acquire weapons of mass destruction to terrorize their neighbors and the rest of the world.

Unlike North Korea, Iran is by no means isolated. Iran exports \$15.5 billion worth of goods each year, \$14 billion of which is comprised of oil. In addition, Iran has approximately \$25 billion in foreign debts, \$12 billion of which was recently rescheduled last year, most of it by our allies.

So those who purchase Iranian oil and those who choose not to compel payment of Iranian debts contribute upwards of \$15 billion to Iran's ability to obtain weapons of mass destruction and to support terrorism.

I fully support the efforts to deny U.S. exports to Iran. For the past 5 years I have sponsored legislation that would deny dual-use technology to Iran. To maximize the impact of the embargo, we must get multilateral cooperation in denying Iran's dual use in military equipment and other items that Iran seeks to purchase.

More important, we must forge multilateral consensus to restrict imports from Iran and to limit the relief of Iran on its foreign debt. We must deny the Iranians resources it needs to support terrorism and to develop weapons of mass destruction.

Our allies must understand how serious we are about Iran. An Iran with a nuclear weapon, a bomb and the means to deliver it is a blueprint for international chaos. It is incumbent upon the administration to apprise our allies on a regular basis of Iran's actions in supporting international terrorism and developing weapons of mass destruction.

Yesterday the President clearly expressed to our allies the need to isolate Iran. The administration must continue to express this position at the highest levels around the globe.

Let me say that as we try to find analogies in history, you can always find analogies for and against every action of an administration, but it seems to me in this post-Soviet era there has been some question about where the United States is to lead the other nations of this planet.

It seems to me there is no better place for America to regain its leadership on issues of international importance than confronting this most terrorist of nations in the world. When Churchill stood up to Hitler, he was alone. It didn't mean that he was wrong. When the United States was among the first nations to stand up to South Africa's racist government, we may have been alone but we were not wrong.

What the administration does in this instance is the right course of action for this country. The Congress needs to make sure the administration works to have our allies join us in this effort, but to give the impression that there is some sort of battle between the Congress and the administration would be I think the worst thing we could do because it will diminish the effectiveness of our own

actions, and it would send a signal to our partners around the world not to join us.

I call on my colleagues to be critical in the sense that we must press this administration to use all of its resources to get other nations to join us, to make sure that the policy is working because the goal of keeping Iran a nation without long-distance missiles and without nuclear weapons and one that stops funding the terrorism that is bringing down the Middle East peace process is among the most important international actions we can take.

Thank you, Mr. Chairman.

Mr. ROTH. Thank you, Mr. Gejdenson.

Everyone's opening statement will be placed into the record, but if there are other members who feel compelled to make an opening statement, I will recognize them.

If not, Representative King, we are waiting for your testimony. Thank you for appearing before our subcommittee today.

**STATEMENT OF THE HON. PETER KING, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF NEW YORK**

Mr. KING. Thank you, Mr. Chairman, Members of the subcommittee. I greatly appreciate this opportunity to testify here today on what I believe to be the absolute necessity of the United States adopting strong, airtight, and unambiguous sanctions against the outlaw regime in Iran.

Mr. Chairman, I know it is your style to cut through the formalities and get right to the basics, and that is what I intend to do.

Iran is an outlaw state. It exports terrorism, it is the major destabilizing force in the Middle East, and it is determined to obtain a nuclear capability.

Mr. Chairman, I was in Israel last week speaking with the highest-ranking officials in the government and in the military. These officials detailed the extent to which Iran funds Hezbollah in Lebanon and Hamas in the West Bank and Gaza. Iran is also the major supporter of the National Islamic Front in Sudan and also supports radical fundamentalist groups attempting to overthrow President Mubarak in Egypt.

Just 2 months ago General Shalikashvili, the Chairman of the Joint Chiefs of Staff, revealed that Iran was deploying Hawk missile systems in the Straits of Hormuz.

Incredibly, as Iran became more and more of a threat to world peace, American oil companies became Iran's biggest oil customers, buying about \$4 billion of Iranian oil annually or more than 20 percent of Iran's total output. The oil companies can make whatever excuses they want, but the shameful truth is they put profits before patriotism and blood money before the national interest.

Mr. Chairman, this is not a partisan issue, and I want to commend President Clinton for his decision to issue an Executive Order restricting American trade with Iran. This is an important first step, but it is only a first step and it does have loopholes.

For instance, U.S. companies can continue to purchase Iranian oil through foreign subsidiaries that operate independently of their parent corporation. Also, of course, foreign companies will purchase the oil which American companies no longer buy, which means that the Iranian economy will not suffer a major disruption.

Mr. Chairman, if the United States is serious about containing and restraining Iran, we must go beyond the President's Executive Order. We must have the will to impose real and meaningful sanctions. That is why I have introduced legislation today which would not only prohibit U.S. companies from trading with Iran, but it would also bar any foreign company which does business with Iran from doing business with U.S. companies. In other words, an airtight embargo.

Mr. Chairman, it would give foreign companies the option. They could deal with Iran or they could deal with the United States, but they cannot trade with both.

Four years ago it took Desert Storm to dismantle the Iraqi war machine which Saddam Hussein had steadily constructed while America and the world had chosen to look the other way. Mr. Chairman, we should learn from our experience with Iraq and we should take preemptive action now to avoid a shooting war with Iran later.

Let America show true world leadership and lead an economic Desert Storm against the terrorist regime in Iran. The stakes for America are too high for us to do any less.

Mr. Chairman, I will be pleased to answer any questions you or any of the members may have.

[The statement of Mr. King appears in the appendix.]

Mr. ROTH. Thank you, Representative King.

For the benefit of the committee Members, let me review the committee's rules for our questioning. We will proceed on the five-minute rule and those members who are present at the start of the hearing will be recognized first in order of seniority, alternating on each side. Then we will recognize the other Members in order of their arrival.

Mr. King, I appreciate your testimony. I know how deeply you feel about this issue, and I think that we all respect people who have the courage of their convictions.

Let me ask you, by imposing this embargo on Iran, the President has now fired the biggest economic weapon in our arsenal. Will this embargo work for us or will it work against us?

Mr. KING. Mr. Chairman, I believe that the President took a right step. I don't think it went far enough. The reason I say that is that it will strengthen the President's hand in dealing with our allies in saying that the United States has taken a tough stand and they should follow suit. The problem is if the allies and the other powers do not follow the President's lead, then it could actually work against the United States because these foreign companies will jump into the breach and they will purchase the oil that American companies are not purchasing.

So that is why I feel that morally and diplomatically it was a strong step by the President, but if he cannot persuade the other powers to go along—and so far there is no indication that they intend to go along—then it could end up working against the United States.

Mr. ROTH. Thank you, again, Representative King, for your testimony, and for your work in this area. We are going to ask Mr. Johnston to see if he has any questions of our witness.

Mr. JOHNSTON. Mr. King, you were very candid in your answer on the fact that the unilateral embargo could backfire on us. We have had a unilateral embargo for a number of years against Cuba and are attempting now to have an airtight embargo, to use your words in your testimony, here. Has that worked against Cuba?

Mr. KING. Mr. Chairman, it has worked against Cuba to the extent that it has weakened the Cuban government, it has weakened Castro, but I think the situation in Iran is different in that Iran's financial situation is very precarious and also what we were attempting to do in Iran is to prevent them from becoming a nuclear power and also to prevent them from being a state exporter of terrorism to radical fundamentalist groups in the Middle East, and I believe, in fact, not just the Middle East but also in countries like Argentina and in certain parts of Europe.

So I believe that an embargo would have the desired impact on Iran because it would prevent it or at least slow down its ability to obtain nuclear capability. It would also certainly make it much more difficult for them to fund and finance groups like Hezbollah and Hamas.

But getting back to what Congressman Roth was asking, if it is just the United States, no, I do not believe it will have a significant effect on Iran, but if we adopt a boycott similar to what I am proposing, an embargo similar to what I am proposing whereby foreign companies if they dealt with Iran would not be able to deal with the United States, that would come close to making it an international embargo, and yes, I believe that would have a very, very strong impact on Iran.

Mr. JOHNSTON. Do you feel a secondary embargo would not violate GATT or NAFTA?

Mr. KING. I don't believe it would, Congressman Johnston. I really don't.

Mr. JOHNSTON. Not NAFTA in this case but GATT.

Mr. KING. No, to the extent that I have been able to study GATT and understand it, I don't believe it would at all, no, and I think that is something that certainly we should pursue.

If it should turn out later on there is a complication, we can address that at the time. But right now I would say, no, it does not, and it is a vital national interest of ours and we should pursue a full and complete embargo and secondary boycott.

Mr. JOHNSTON. Last question, Mr. Chairman. I know this is not the subject matter, but your comment is that the embargo against Cuba has weakened Castro. In what way has the embargo weakened Castro?

Mr. KING. Well, to the extent that it has isolated them in the world, certainly it is no longer funding military operations in Angola or other parts of the world or even Central America or South America.

Mr. JOHNSTON. Do you think the embargo did that?

Mr. KING. I think the embargo certainly had something to do with it, yes. Obviously the collapse of the Soviet Union had something to do with it also, but I think the embargo had an impact. I would make a distinction between the Cuban embargo and the Iranian embargo.

Mr. JOHNSTON. I would, too, with the exception of Mr. Roth's I think brilliant statement which said there was a failed policy for 16 years and a unilateral embargo does not work. I don't see any difference in a unilateral embargo, Mr. Chairman, against Iran as compared to one against Cuba.

Thank you.

Mr. KING. Again, Congressman, that is why I am urging a complete embargo, not a unilateral embargo.

Mr. ROTH. Thank you, Mr. Johnston.

Mr. Kim, we will call on you for your questions.

Mr. KIM. Thank you, Mr. Chairman.

I would like to ask a few questions about this sanction. It seems like whenever we get into trouble, we always talk about sanctions, sanctions against North Korea, sanctions against China. Are there any other alternatives other than sanctions?

It seems like we are trying to gain a political goal at the expense of businesses. Who is going to be hurt by imposing sanctions? I think perhaps Iran and our businesses, too.

Can you think of anything else besides sanctions?

Mr. KING. I would be willing to entertain any proposals anyone has, but as I have studied this situation in Iran, Iran being a terrorist nation, what cash it gets, what funds it gets it uses to fund international terrorism. It is clearly the major destabilizing force in the Middle East, and I don't see any alternative to it other than military, which no one is advocating, and we shouldn't, but this is a clear case, I believe, where sanctions are appropriate.

I don't think sanctions should be used across the board. I think sanctions are, as Congressman Roth said, the major weapon the United States can fire, and it should only be done in the rarest circumstances.

I believe, though, that this is a particularly unique circumstance where an embargo would have a real effect because otherwise what we are doing is the funds are going to continue to go into Iran, Iran is going to continue to consolidate its power, and it is going to use that power and those resources. Again, we are talking about Sudan, we are talking about Algeria, we are talking about Egypt, we are talking about Lebanon, we are talking about Palestinians.

I can't emphasize enough, when I was in the Middle East last week, the extent to which the Israeli leadership, when you are talking to the Egyptian leadership, the extent to which Iran is becoming more and more of a lethal threat in the Middle East, not just the peace process, but to the security of countries in the Middle East which are completely within our strategic area of importance, our zone of interest.

And again, Jay, I would be more than willing to listen to any options anyone has other than sanctions. I see none other at this time. And obviously I don't want to minimize the fact that this will have some impact on the American economy. There is no doubt about it. But I think we saw in Desert Storm what happens, or with the buildup in Iraq when America does not take action, the price we pay later would be greater than the price we pay now. The price we pay later could be in blood. The price we have to pay in the short term could be in dollars. I think when you balance the

two of them, I would rather take economic action now than be forced to take military action later on.

Mr. KIM. Thank you.

Mr. ROTH. Mr. Gejdenson.

Mr. GEJDENSON. Thank you, Mr. Chairman.

I think it is a very tough situation since it is going to take some stick-to-it-iveness, and that is not a trait that we Americans tend to have. There certainly were times in the decades of struggle against the racist regime in South Africa where people said that the embargo wasn't working.

It is clear that you have to have a long-term view here, and when some people on this committee would say, Why did we pick on South Africa when it was not the only government taking actions that were wrong, we said we thought it was one of the worst. And we took South Africa on because of all the nations of this planet, it had a policy that was racist to a degree which few other countries had, and the world community after a time joined us.

It is to me the same instance here, that in Iran—there are other outlaw countries. There are few who have financed as much terrorism and present as significant a danger to America's interests as Iran does.

When you talk to the people directly involved in the Middle East peace process, the continued support for extremist groups that execute people on both sides of the border, Israel and where the Palestinians are, the single greatest threat to the peace process isn't the commitment of the Palestinians nor the Israelis, but the threat from financed terrorism that continues to kill people on both sides.

So I think that, you know, there are embargoes that work, there are embargoes that don't work. There are situations that we can solve quickly, frankly, like the Gulf War as it turned out, but there are some situations where America's interests will have to be steadfastly maintained.

I would say to Mr. King, and I appreciate your support for the President's actions, I have two concerns. One is, I do have a concern with secondary boycotts, and I hope to go back and look at your legislation and fine tune it. There are a couple of areas where I think there are unintended consequences, and frankly, if an Iranian national would own a 7-Eleven out here in your district, Virginia or anywhere else, if an American citizen bought a Big Gulp there, which is I guess one of their drinks, they would be at this point punishable by a \$10,000 fine. I know that is not your intent. The same would be if an American company that exported chairs or office furniture sold something to a company or an individual in France that was doing business with Iran.

So I think what you need to do, and I think your intent is the right intent, I think we want to make sure that there aren't unintended consequences. And what we have to do as legislators jointly is I think work with the administration to try to get them to put every effort on getting our allies to join us.

It is not enough for the administration to simply draw the line in the sand and consider its job done. The administration is going to have to use its resources and its very top-level people to pursue our allies as we had to do so often in the past. You only need to read a little history on how things could have been different if

there wasn't a Berlin airlift, if there wasn't the resolve of President Kennedy with the missiles in Cuba, if there wasn't the resolve of administration after administration against the Government of the Soviet Union, and frankly we are lacking some of that resolve today because it doesn't appear to be an imminent military threat to the United States.

If there is a threat to the United States today of a military and political nature, it is Iran. There is no question it threatens world peace, and we need to continue to work with the administration and people like Mr. King to try to make sure that it is a policy that works.

Thank you, Mr. Chairman.

Mr. KING. If I could just comment on Mr. Gejdenson's remarks. Certainly I agree with the entire thrust of his remarks.

I would say that this is one time, South Africa was another, where the moral dimension of American foreign policy coincides with the real policy. It is morally right for us to impose sanctions; it is also in our strategic best interests to do so.

As far as the unintended consequences, when I was in law school I was always accused of unintended consequences in my legislative courses, so I wouldn't be surprised that there may be some in this bill. I certainly would work with you and the subcommittee in trying to eliminate any of those, but I think we have to be careful not to allow a concern about a 7-Eleven store to get in the way of an overall policy. So I think while there may be certain semicolons and commas that have to be adjusted or readjusted, we have to keep our eye on the ball, and I think the end result should be to seek universal, air-tight-sanctions on Iran.

Mr. ROTH. Any other Members of the committee who would like to ask our colleague a question?

If not, thank you very much, Mr. King, for your excellent testimony and your commitment to this particular issue.

Mr. KING. Thank you, Mr. Chairman. I appreciate the opportunity. It is always a pleasure to work with you. Thank you very much.

Mr. ROTH. Thank you.

Under Secretary Peter Tarnoff, who had planned to testify, has been called away by the President to help implement the new sanctions. But we are very pleased to have with us today Mr. Robert Pelletreau, Assistant Secretary of State for Near East Affairs. Mr. Pelletreau is in overall charge of the administration's Middle East policy.

Mr. Pelletreau, please proceed.

STATEMENT OF ROBERT H. PELLETREAU, ASSISTANT SECRETARY OF STATE FOR NEAR EAST AFFAIRS

Mr. PELLETREAU. Thank you, Mr. Chairman. I am pleased to join you as we discuss our efforts to make the Government of Iran pay a price for its objectionable behavior.

Two days ago President Clinton boldly projected American leadership in holding Iran accountable for its unacceptable policies. On Sunday, the President announced his decision to issue an Executive Order banning all U.S. trade with and investment in Iran, including the purchase of Iranian oil by American companies abroad.

These new sanctions, in conjunction with our existing set of restrictions, will create a U.S. embargo against Iran.

This was not an easy decision. It was the culmination of a painstaking review of our Iran policy. This action was chosen carefully to advance those strategic U.S. interests challenged by Iran's outlaw activities. Our core concerns include thwarting terrorism, advancing the Arab-Israeli peace process, fighting the spread of nuclear weapons, and maintaining security in the Persian Gulf.

By sending a powerful political message to those who may have doubted the importance we attach to these interests, the President's recent decision will strengthen our hand as we again urge other nations to adopt our approach toward Iran. His bold action underscores America's readiness to lead by example.

Only by imposing a real and heavy price can we and other countries convince the Iranian leadership that changing its threatening behavior is in Iran's own interest.

The President is expected to sign the Executive Order very soon. The new ban will augment what was already the toughest set of existing restrictions against Iran in the world. It will prohibit trade with Iran by U.S. companies, including overseas trade in Iranian oil, and U.S. investment in Iran.

These new sanctions were designed to build on our current prohibitions on the imports into the United States from Iran and on exports to Iran of sensitive goods. They will also expand the prohibition, imposed by the President in March, on U.S. financing and management of the development of Iran's petroleum resources.

The impact of the President's decision will be strong. Notably, the Executive Order will eliminate trade in Iranian oil by U.S. companies and their overseas branches. Last year U.S. companies and their affiliates purchased more than 20 percent of Iranian crude oil exports.

It will also eliminate U.S. exports to Iran. Those sales amounted to \$326 million in 1994. It will ban the reexport of certain sensitive U.S.-origin goods. Finally, it will prevent any investment in Iran by American firms and their overseas branches.

We know that these steps will result in some costs to U.S. firms and workers. We will do what we can to limit the adverse impact. We are convinced, however, that an embargo is the most effective way our Nation can achieve its goal of pressing Iran to abandon its drive to acquire devastating weapons and its support for terrorist activities.

The President's decision to impose additional sanctions is grounded in a policy established in the early days of this administration. With the President's support and under Secretary Christopher's stewardship, this administration has accorded a high priority to American efforts to exert economic and political pressure on the Government of Iran so as to compel a change in its threatening behavior.

To maximize the pressure, we have worked along a dual track, applying unilateral restrictions and seeking multilateral cooperation in pressuring Iran. We have had some important successes, but found nonetheless that Iranian behavior in some areas of concern has worsened. These disturbing trends led the Secretary to recommend to the President that he take new steps.

Let me outline the areas of concern. In particular, Iran's support of violent groups that conduct terrorist acts to undermine the peace process has increased. In defiance of the international community, the Iranian Government maintains ties to rejectionist groups like the Palestinian Islamic Jihad, Hezbollah, and Hamas, each of which has received funds, weapons, training or logistical support from Iran.

The Iranian Government has also intensified its efforts to develop weapons of mass destruction. These efforts, as well as Iran's conventional military buildup, warranted additional review.

Like Congress, we have found reports of Russia's agreement to engage in nuclear cooperation with Iran particularly disturbing. Given Iran's petroleum reserves, the Tehran government's desire to obtain gas centrifuge equipment, as well as nuclear power reactors from Russia, only bolsters our conviction that Iran seeks to develop its nuclear weapons capability. Iran has also sought to acquire light water nuclear power reactors from China, and Beijing has announced its intention to go through with such a sale.

Iran's persistent pattern of support for outlaw activities led us inexorably to the following conclusion: Worsening Iranian behavior demands a response. Iran must pay a price for flouting the norms of law-abiding nations.

In taking the decision to ban all U.S. trade with and investment in Iran, President Clinton clearly signaled American determination to lead the effort among the international community in holding Iran accountable for its actions. He also intended the Government of Iran to understand our seriousness of purpose. We hope our action will cause the Iranian leadership to review its policies, especially support for terrorism and the pursuit of weapons of mass destruction, and to question whether they truly serve Iran's interests.

In making his decision, the President carefully considered the economic costs and the national security benefits of an embargo. He determined that if we are to succeed in getting other countries to make sacrifices in order to change Iran's behavior, we, too, must be willing to sacrifice. As a world leader, the onus lies on us to mobilize support. The President's bold step has reinforced our ability to secure the cooperation of all nations that share our interest in international peace and security.

Secretary Christopher has already begun to redouble our diplomatic efforts with key countries to maximize multilateral support for pressuring Iran. He is sending personal messages to our diplomatic partners, calling on them to review their economic ties with Iran. He is also asking them not to permit their firms to fill the void left by American companies.

In June, when the G-7 next meet in Halifax, the President will again urge G-7 leaders to adopt our approach. He will convey the high priority we attach to containing Iran, reiterate our mutual interest in changing objectionable Iranian behavior, and stress the need for multilateral cooperation. The President's decision will also serve as a strong basis for us to once again press the Russians and the Chinese to forego nuclear cooperation with Iran.

U.S. policy toward Iran has long been characterized by strong bipartisan support. Similarly, there is general agreement among the industrialized countries on the need to bring about a change in

Iran's unacceptable policies, although there have been differences on the best tactics to use to reach this goal.

For example, some of the allies have argued that constructive engagement will moderate Tehran's behavior. We disagree. We believe concessionary economic policies will encourage the leadership in Tehran to think it can improve relations with the West without changing its unacceptable policies.

In recent months, some allies have pointed to U.S. economic ties with Iran, despite the heavy unilateral limitations on this trade, as justification for maintaining and expanding their own commercial relationships. The President's decision will eliminate that excuse and place the United States in the strongest position to encourage other nations to adopt similar or parallel steps.

Iran cannot stand up to coordinated pressure from all the industrialized nations. That is exactly the goal of the Executive Order, to increase the effectiveness of our efforts to maximize pressure on Iran.

As we seek the broadest possible multilateral support, we must be careful not to jeopardize our own bilateral relationships with other industrialized nations, particularly with the G-7. In the course of our review of Iran policy, we examined the issue of extraterritoriality and a ban on financial transactions.

In terms of the extraterritorial application of U.S. law, we concluded that the risk of alienating countries, whose cooperation we need to maximize the effectiveness of our policy toward Iran, outweighs any potential benefit. Our policy would not be served by launching a series of drawn-out legal battles with our closest friends. We want to isolate the Iranians, not become isolated ourselves.

We also determined that a prohibition on all financial transactions would undermine our role in international banking. Such a ban would interfere with Iranian payments to Americans pursuant to awards rendered by the Iran-U.S. claims tribunal in the Hague. It could prevent us from meeting our obligations under the Algiers Accords, which ended the 1979-1981 hostage crisis, and other international agreements. By contrast, our ban on investment will prevent financial transactions that could help stabilize Iran's economy without running these risks.

Mr. Chairman, the administration believes it is essential to sustain the close collaboration the Executive Branch has shared with the Congress on the issue of Iran policy. We welcome opportunities, such as today's hearing, to consult with you on this important matter.

We believe the President's decision to impose additional sanctions on U.S. trade and investment with Iran will dramatically reinforce American leadership in urging our diplomatic partners to join us in pressuring Iran to change its objectionable behavior. We believe our policy deserves the support of our allies, and we hope they will respond to our lead. We hope, too, that the President's bold action will command the backing of Congress.

Thank you, Mr. Chairman.

[The statement of Mr. Pelletreau appears in the appendix.]

Mr. ROTH. Well, thank you, Secretary Pelletreau. We appreciate your testimony.

Our committee members do have questions for you, but before we go to that, I would like to welcome our Chairman of the full committee, Mr. Gilman.

I think if you would like to have a statement, Mr. Chairman, we would be happy to hear it.

Mr. GILMAN. I would like to make a few remarks. I want to welcome Secretary Pelletreau for appearing before the committee.

I would like to compliment, Mr. Chairman, the Economic Policy Subcommittee that you chair, and my colleague Peter King from New York for his leadership on this important issue.

The President's announcement of additional sanctions against Iran would not have been possible without sustained pressure from Congress, including members from this committee, and I would like to voice my strong approval of the actions of the President to prohibit trade and investment with Iran.

Stopping the trade by U.S. companies in Iranian oil is a critical first step in our efforts to try to isolate this terrorist regime, but it is only a first step. The administration has finally begun to transform its rhetoric into a realistic approach, to limiting the ability of this one country to finance terrorist activities. It is a beginning and not the end of the process.

The administration must now move to ensure that foreign companies don't take our place in buying oil from Iran. We must establish a comprehensive set of prohibitions, preventing foreign subsidiaries from simply replacing our own companies.

The administration also must make clear that our companies will be barred from taking any oil from non-American companies that may have increased their own purchases from Iran with an eye to reselling it on the American market.

This administration also needs to stop making promises about multilateral cooperation against outlaw nations. Instead, it needs to begin demonstrating that it is able to harness the G-7 framework to an Iran-centered control regime for arms, for nuclear technology, for terrorist control items, and all dual-use technology that can help Iran to develop weapons of mass destruction.

We certainly shouldn't be waiting to dot the i's and cross the t's for a global proliferation regime while Iran is rushing head long toward a nuclear capability. Now the administration should expand its newly announced economic package on Iran into a comprehensive multilateral framework that will include all of our G-7 partners. And while the administration is laboring to fashion a comprehensive coherent policy, our trading partners in Europe and Asia must also understand the risks they run in refusing to recognize Iran as the terrorist regime that it is.

If our allies believe that in trading with Iran at the expense of our own Nation, they can reap a short-term profit, they should know that there will be a long-term cost to our relationship and our alliances.

In the 1930's, many leading European politicians believed they could do business with Hitler. In September 1939, they learned to their dismay just how wrong they were.

As we celebrate the 50th anniversary of the defeat of Nazism and Hitlerism, let not the seeds be sown for more acts of terrorism and threat of a nuclear-armed Iran.

Thank you, Mr. Chairman.

Mr. ROTH. Thank you, Chairman Gilman. Let me ask you this, do you have any other questions?

Mr. GILMAN. Just one question, Mr. Chairman. I thank you.

In the event that our friendly nations do not abide by our sanctions, what actions can we take to try to make our sanctions effective?

Mr. PELLETREAU. We think that these additional sanctions that we are putting in place through the President's Executive Order will strengthen our ability to bring about much greater cooperation. It will depend on how we work out with each of the states of the G-7, with Russia and with China. But we intend to make a very strong effort to put in place very strong multilateral cooperation against Iran, and we believe the best way to do that is through seeking their cooperation, sharing our intelligence with them, engaging in comprehensive dialogue with them, and showing them by example and taking the high ground and the moral leadership which way we all ought to go as a collective international group.

Mr. GILMAN. Thank you, Mr. Secretary.

Thank you, Mr. Chairman.

Mr. ROTH. Thank you.

Mr. Secretary, I want to follow up on that comment. I have here a Reuters report which moved on the wire at 11:20 Washington time, just a few hours ago. It seems that France, the United Kingdom, and the European Union all have flatly rejected any participation in the U.S. embargo. Germany said the embargo is inappropriate. The German economic minister said that he had not even been consulted in advance.

Now, Mr. Secretary, my question is this. If the test of the U.S. embargo is whether others go along, then already you have three strike-outs. What is your response? Can it be that we did not consult, for example, one of our allies, Germany, before we announced these sanctions? Is that true?

Mr. PELLETREAU. No, that is not true. We have had an existing dialogue with Germany since the beginning of this administration on how we should react as responsible members of the international community toward Iranian actions, and we have reached agreement in some areas. We have reached agreement that we should do nothing that would allow Iran to acquire technologies that would support weapons of mass destruction.

Mr. ROTH. That does not answer the question. The question I have is this: These countries that I mentioned—France, United Kingdom, European Union—all have flatly rejected participation in the U.S. embargo, and the German economic minister said he had not even been consulted in advance on the embargo? That is the question.

Mr. PELLETREAU. They were not informed in advance of the precise terms of what the embargo would consist of. However, they were certainly aware that the United States was studying additional measures and was looking to them to take additional measures as well.

Mr. ROTH. That is a far cry from consulting with people on the embargo. I mean, if we need all these countries on our side, and

we don't even consult with them before we impose an embargo, that doesn't seem the proper action to take.

Mr. PELLETREAU. Well, the embargo is an action that is taken against our own companies, and we are now going to them to continue and to strengthen the dialogue that we have with them.

Mr. ROTH. That is precisely the question we have. We end up shooting ourselves in the foot. We are just going to hurt our own companies and not in any way have an impact on Iran. Other countries, whether they are Japanese or German or British, are all going to go in there and pick up additional markets. Yesterday the White House acknowledged publicly, for example, that we are going to lose several thousand American jobs because of these sanctions.

Now, these sanctions originated with the State Department. Incidentally, if the State Department is so dedicated to this embargo, where is Secretary Christopher? We invited him here. This is a big step. Where is he? They sent you down here, and you are a good man, Secretary Pelletreau, but you are not the Secretary of State. If this is such an important policy, where is he?

Mr. PELLETREAU. He is out working to persuade our allies that they need to help go along with this.

Mr. ROTH. It seems to me he should have been doing that before we imposed the embargo.

Now, the French foreign minister suggested to the United States today that the United Nations should have been consulted before we imposed these sanctions. Why didn't we do that?

Mr. PELLETREAU. We had no indication that we would be able to be successful through the United Nations.

Mr. ROTH. Well, we will ask Mr. Gejdenson for his questions. We are on the 5-minute rule.

Mr. GEJDENSON. Thank you, Mr. Chairman.

I am glad to see the Chairman has joined those of us in the Congress who support the United Nations. When we have additional markups dealing with U.N. peacekeeping and other issues, the Chairman will join us in the support of this international organization. I think the U.N. is a worthy organization for our involvement. I am glad to see the Chairman has joined that side of the aisle.

I think the danger in starting off depending on which of our allies support us, Mr. Chairman, is that frankly that would allow the United States only to engage in policies that we start off with a win, and frankly the tough ones don't start out that way. And I think that this is a very challenging situation, but I think it also provides us for opportunities in trade.

One of the things that has frustrated me through the years is frankly some of the trade restrictions we have had on friendly, pro-American countries that don't involve themselves in terrorism, and it seems to me the focus always should have been on countries that were bad guys and try to isolate them.

I think we are heading for the right policy here. I think a policy that leads the international community to tighten its dealings with terrorist nations will enable us, frankly, to decontrol more of the technology to nations that don't provide a threat for us.

Let me ask you, sir, a few questions. You may not have all the answers with you. I don't expect you to, but—and some may be classified and have to be given to us in another format.

From where Iran is today, what do you think the cost of Iran in dollars and in time if things, if we don't slow them down, how much more money do they need to spend and how much time will it take them to be nuclear ready and missile ready with systems that can deliver nuclear weapons if they are not further restricted?

Mr. PELLETREAU. The then-CIA Director Jim Woolsey testified in 1993 that it could take Iran around 10 years to become a nuclear weapons state. That will obviously be shortened to the extent that Iran is able to secure cooperation from any nuclear supplier.

It can be lengthened to the extent that we are able to impose a comprehensive embargo on any form of nuclear cooperation with Iran, whether it is for civilian so-called peaceful reactors or for a direct acquisition, and that is what we are working on doing with the Russians and the Chinese, to persuade them that any form of nuclear cooperation with Iran is against their own long-term interests.

Mr. GEJDENSON. You know, I would note that in Congress and across the Nation following the tragic situation in Oklahoma, there has been obviously a marked focus on security and the cost of some of the terrorist activities, domestic or otherwise. I would hope that all viewing this policy would think about the debate that would ensue following a detonation, either for demonstration purposes or against one of its adversaries, by Iran of a nuclear weapon.

Now, if that estimate is still accurate in the range of 8 years away from having that capability, what about the cost? Do we have any sense of how much of their GNP they have to divert, what kind of dollar costs that program would have?

Mr. PELLETREAU. I don't have an accurate estimate, but it is certainly in the billions of dollars.

Mr. GEJDENSON. If you could get that to me, I would appreciate it, and just get a sense of the magnitude of dollars a country has to commit to be able to develop a nuclear weapon.

A second part of this process, of course, will be to convince countries like Russia who are in dire economic condition that there are economic alternatives, and frankly that will be very challenging when dealing with the Congress because a number of our colleagues understandably are concerned about any program that uses taxpayer dollars.

But it seems to me that one of the ways you get Russia, which is in very tough economic shape, is to give them some other economic opportunity that is more attractive than building a nuclear facility for the country of Iran.

Is the administration examining those options?

Mr. PELLETREAU. Yes, we are examining options that would provide incentives as well as sticks.

Mr. GEJDENSON. Mr. Roth brought up the prospect of a U.N. action. Is it appropriate to find a U.N. format for furthering this discussion? Because I believe that we do need to press this at every opportunity and every forum that presents itself. So do we have any plans for taking action at the United Nations?

Mr. PELLETREAU. With respect to the Russian reactor, we have not been pursuing it through the U.N.

Mr. GEJDENSON. The question was towards isolating Iran.

Mr. PELLETREAU. Thus far our soundings indicate that we do not have a unanimity of view with respect to possible resolutions of the Security Council against Iran, no such resolutions exist.

Mr. GEJDENSON. It seems to me—and I will finish with this—that one of the things we need to do there, we need to press our allies at every level, the major allies and the other countries, and other countries around the world that don't find themselves aligned with us on a regular basis. This is an issue that has to be addressed because it is an issue of international security, it is an issue that directly affects the peace process, the lessons, and what happens out of Iran will have an impact on the subcontinent between Pakistan, India and all across the globe.

This is a very serious and important policy, and I hope the administration continues with every bit of its effort.

Thank you, Mr. Chairman.

Mr. ROTH. Thank you, Mr. Gejdenson.

Mr. Kim, and then we will ask Mr. Rohrabacher and Mr. Bereuter for their questions. Mr. Kim.

Mr. KIM. Thank you, Mr. Chairman.

It is kind of puzzling to me that despite our objections last winter, Germany and Switzerland resumed export guarantees for Iran. It sounds like expanding trade to me. Plus, OECD countries rescheduled about \$12 billion in debt over the last year. Obviously they don't respect our decision. We have strong objections, but they did it anyway.

Why do those nations have no respect for our decision, what makes you think that they will join us now, after the fact? I was wondering why we didn't go to the U.N., and ask for a unilateral U.N. grievance sanction, rather than take such a bold action.

Mr. PELLETREAU. We have engaged in a dialogue with the European countries, with Iran's major creditors. When Iran got into a situation in 1993 when it couldn't service its debt, we were successful with our European partners in preventing a multilateral Paris Club rescheduling, and over 1994 we were able to delay a lot of the individual rescheduling negotiations. But as you pointed out, a number of nations went forward, often under pressure from their own companies and suppliers, to reschedule, and in some cases there have been extension of small amounts of additional credit.

I think our policies up to this point had some effect in restraining those nations, but we were not successful in having them cut off the extension of additional credit. They would point out, for example, that your U.S. companies are doing plenty of business with Iran. They will no longer be able to make such an excuse. We intend to go at them harder and higher from the President on down to broaden the whole fabric of containment against Iran.

Mr. KIM. I am not convinced. It seems like this essentially will hurt us more than it will hurt Iran without our allies support. Looking at the historical pattern, obviously they have no respect for our judgment. I don't know what makes you think that they will join us now.

Mr. PELLETREAU. The purpose is to bring about a change in Iranian policy, and our actions immediately have both political and economic impact on Iran. That impact will be strengthened to the extent that we can get our allies to go along with us, and it doesn't

mean in every case that they would necessarily adopt exactly the same measures, but in each case we are asking other countries to review their economic relationships with Iran, to tighten those economic relationships, and to join us in convincing Iran that it must abandon terrorism and abandon the search for the devastating weapons of mass destruction.

Mr. ROTH. Mr. Rohrabacher.

Thank you, Mr. Kim.

Mr. ROHRABACHER. Mr. Chairman, Mr. Secretary, I usually find myself in disagreement one way or the other with the administration, and in this case the policy seems to be somewhat in the right direction, but the process seems to be way off the mark.

I worked at the White House for 7 years. The fact that our allies were not notified prior to the announcement of this embargo is unforgivable, and if you really were serious about it, that should have happened. During the administration when I worked at the White House, we had Geoff Kemp, who was notifying our allies all the time, talking to people, and making sure that these things were done right.

But let me get down to the policy instead of the process. Iran is an extremely oil-rich society. They burn gas. Is there any question in your mind that the Iranians are trying to obtain nuclear power plants when they have got all of this other kind of energy, but they are just trying to get these nuclear power plants specifically to increase their weapons capabilities, their nuclear weapons capabilities?

Mr. PELLETREAU. That is true. With Iran's tremendous petroleum reserves, they have no need for nuclear power to provide their civilian power needs.

Mr. ROHRABACHER. So this is a threat aimed directly at the rest of the world when you have a belligerent Third World power that has all the energy they want, and now they want to obtain nuclear energy facilities basically in order to build bombs; isn't that correct?

Mr. PELLETREAU. I think that is correct. I think there is no justifiable rationale for seeking nuclear reactors.

Mr. ROHRABACHER. And there is a justifiable reason, then, why we should be concerned?

Mr. PELLETREAU. Absolutely.

Mr. ROHRABACHER. I appreciate that you are here, and I appreciate that the administration is trying to focus on it. I don't quite understand why the Iranian government feels that it has to maintain a belligerency with the United States. I believe that we have reached out time and time again to the Iranians, and they have seemed to want to slap our hands or threaten us every time we do; isn't that correct?

Mr. PELLETREAU. That is true. That has been the case since the Iranian revolution occurred, and the United States was labeled "the Great Satan." Every year there are demonstrations against the United States in Iran. It is one of the ways, I think, that the existing regime stays in power.

Mr. ROHRABACHER. There have been many reports that the Iranian government is involved in counterfeiting American money,

specifically \$100 bills. Have you received any credible reports that the Iranians are counterfeiting American money?

Mr. PELLETREAU. I am sorry, I would have to give you a response for the record on that.

Mr. ROHRABACHER. Well, I think that is a significant answer. Then the administration is not confirming or denying that it is possible that the Iranians have been counterfeiting billions of dollars, thus threatening the economic stability of the American currency?

Mr. PELLETREAU. I know there is an intense investigation and campaign under way led by the U.S. Secret Service to uncover all the sources of counterfeiting of American currency abroad. I just am personally not in a position to give you the exact details of what we believe Iranian involvement is in that, and I will be happy to do so.

Mr. ROHRABACHER. Rather than the exact details, why don't you give me some general details. Is this administration operating under the assumption that the Iranians have been counterfeiting American currency?

Mr. PELLETREAU. I am just not sure enough of my answer to be able to give you a definitive answer here, and I will provide one.

[The information appears in the appendix.]

Mr. ROHRABACHER. Mr. Secretary, I just arrived, as many of our colleagues when we have a break—we go to different places in the world to try to get a feel for what is going on overseas. There are many leaders throughout the world, especially economic leaders, who believe that the American currency is being undermined by an intentional act of economic warfare on the part of the Iranian government to undermine the currency of the United States by counterfeiting billions of dollars worth of U.S. currency.

Am I getting it right that basically you are not denying that this is going on?

Mr. PELLETREAU. I am not denying it.

Mr. ROHRABACHER. If this is the case, is this act of economic warfare on the United States part of the administration's decision to place this embargo today?

Mr. PELLETREAU. I certainly think that would be an additional strengthening argument for our activities, yes.

Mr. ROHRABACHER. I would hope that the people of Iran understand that the people of the United States would prefer to be on friendly terms with their government and on friendly terms with the people of Iran. There is absolutely no reason why we couldn't be the best of friends, and I am absolutely disturbed by the fact that you have a regime in Tehran that feels it necessary to obtain nuclear weapons and to declare economic war on the United States of America.

This is what we are hearing today, and the administration is trying to act, and to the degree that this is a challenge to our national security and our economic well-being, you will have the support of this Congressman and I am sure those people on this side of the aisle.

Thank you very much, Mr. Secretary.

Mr. PELLETREAU. Thank you.

Mr. ROTH. Thank you very much, Mr. Rohrabacher.

Mr. Bereuter.

Mr. BEREUTER. Thank you, Mr. Chairman.

Secretary Pelletreau, thank you very much for your testimony. Dr. Schott, who will testify later, has written testimony that expresses skepticism about whether the administration is likely to be successful—I will put it that way—without really having close support from our normal allies on the embargo action and certainly much less likely to have cooperation from China and Russia.

I was looking at trade statistics the last year for which they are available, Iranian imports from their top 20 trade partners. In that period of time, they imported \$10.871 billion from the top 20 countries. We sold them \$616 million worth of exports, which really is only about 6 percent of the total.

Mr. PELLETREAU. That would have been 1993, I believe.

Mr. BEREUTER. That is correct. That is only 6 percent of their total imports.

So it would seem if we are going to have cooperation among some of the nations that really provide the most—Germany in that year provided four times as many exports to Iran than the United States, Japan and Italy doubled the United States total, France and the United Kingdom also supplied more of the Iranian imports during that period of time, and of course that is affected by the fact that we stopped taking any of their exports at all in terms of the overall trade balance.

So I think that Chairman Roth has a point. We really need to have multilateral cooperation on this embargo if it is going to be effective.

Those figures are pretty striking, aren't they?

Mr. PELLETREAU. Yes, they are, and we have had an ongoing dialogue. We have had a certain amount of cooperation. We believe that taking the measures that the President has announced will give us the ammunition to increase that cooperation on behalf of our allies and the other countries that you cited there.

Mr. BEREUTER. I was looking at the composition of their imports, and manufactured products are by far the largest amount of their imports from the 20 top countries, well over \$9.5 billion. Food-stuffs, raw materials is \$1.2 billion, so that is not where most of it is at this point.

I just want to express my concern that, as Chairman Roth said, we didn't nail down a multilateral embargo before we proceed. I know that is not always easy, it is usually not, but if it is going to be effective, it seems to me it has to be perceived that way.

Thank you very much for listening. I hope you take our concerns and our best wishes for a very energetic effort, even if it is retroactively, to bring on our partners to this embargo. Otherwise, I think it is close to futile.

Mr. PELLETREAU. Thank you.

Mr. ROTH. Well, thank you very much, Mr. Bereuter.

We are going to ask Mr. Chabot for his questions.

Mr. CHABOT. Thank you, Mr. Chairman.

I share my colleague's concerns that perhaps the administration hasn't taken sufficient action to get our allies' cooperation before announcing this embargo. That concerns me.

Assuming that our allies do not join us in this embargo, are there any examples that you can give us where unilateral action

by this country against other countries who were carrying on activities that we frowned upon actually worked?

Mr. PELLETREAU. Well, we began, for example, with unilateral action against Iran in the case of denying Iran any kind of equipment or technology that would contribute to programs to develop weapons of mass destruction. We began domestically with a unilateral embargo. We then went to our allies and we were unable to present—

Mr. CHABOT. Excuse me a moment. I am talking about other countries.

Mr. PELLETREAU. Well, I thought I was trying to give you an example.

Mr. CHABOT. I am talking about another country that we had difficulties with and there was a unilateral embargo.

Mr. PELLETREAU. We will think on it and see if we can find you some examples.

Mr. CHABOT. Okay, I appreciate that.

[The information appears in the appendix.]

Mr. CHABOT. In addition, relative to the Soviet Union and their selling equipment or materials to Iran which could be used to produce nuclear weapons, what action do you anticipate or what will be our policy relative to the Soviet Union should they decide not to cooperate?

Mr. PELLETREAU. We are going to continue and make an even greater effort to persuade them that they should not be involved in any type of nuclear cooperation with Iran. The contract that they are in the process of negotiating is a contract between the Ministry of Atomic Energy and Iran. There are other centers of power and other centers of decisionmaking in Moscow, and we are approaching them all with a major educative effort, with sharing of intelligence, and with trying to persuade each of these Russian leaders that this is a shortsighted course, and it should be reversed. There is not a drop dead point or a cutoff point. This is an effort that we are going to continue to be engaged in until we achieve success.

Mr. ROTH. Will the gentleman yield for a second?

Mr. CHABOT. Yes, I will.

Mr. ROTH. Mr. Chabot, thank you for yielding.

Don't hold your breath waiting to be successful with the Russians. I just had lunch with several Russian officials, as did some of our other colleagues, at 12:30. They just talk in circles. They are going to go right back to selling everything they can to Iran. I don't think you are going to have much success there.

Thank you for yielding.

Mr. CHABOT. Thank you.

How optimistic is the administration that any of our allies will join us in this effort?

Mr. PELLETREAU. I think it is a question of the extent to which our allies join us. Our allies have joined us up to a point. We are going to press them to join us further and to tighten their own economic restrictions on Iran further. I can't tell you how far they will go, but every turn of the screw is an additional turn against Iran by every country, and each country will have to make its own deci-

sions, but we seek a very tight international economic constraint on Iran, on dealing with Iran.

Mr. CHABOT. I guess just what we are hearing here or at least my sense is that whereas we all are outraged by Iran's policies and the actions that they have shown thus far, I think it is absolutely critical that we have our allies' cooperation in this, or in effect what we do is we harm U.S. business and don't accomplish what the objectives are here. I think that is a concern that we all have.

Thank you.

Mr. ROTH. Thank you very much, Mr. Chabot, for your questions.

I am going to call on Mrs. Meyers for any questions she might have.

Mrs. MEYERS. Thank you, Mr. Chairman.

You have said that we didn't approach our allies through the U.N. to try to get some support because we didn't have any indication we would be successful. What kind of further information or further activity would make it possible for us to approach through the U.N.? Do we foresee doing that in the near future?

Mr. PELLETREAU. I don't really foresee doing that in the near future. I think our effort is going to be aimed at the G-7 in particular. We are looking to the Halifax Summit. We are taking some actions right now leading up to the Halifax Summit that are led by the Secretary, and of course the President will be engaged personally in that.

Mrs. MEYERS. I think we have suspected that Iran has run many of its terrorist activities out of its embassies around the world. Have we asked any of our G-7 partners to declare the personnel in the embassies persona non grata in their countries?

Mr. PELLETREAU. We have certainly called their attention to the activities of Iranian agents acting in different embassies around the world. I don't believe we have asked anybody to close an embassy.

Mrs. MEYERS. I guess what I am leading up to is if our friends have not indicated a willingness to join us in this embargo, have they indicated that there is anything that they are willing to do to assist us in this?

Mr. PELLETREAU. Yes. Up to this point we have agreement by all the G-7 that we will not provide any supplies or technology that would help an Iranian nuclear weapons program or a biological or a chemical weapons program. We are in general agreement that we should not provide high-tech weapons or dual-use high tech that could go to helping Iran in that way.

We have had some success in retarding the amount of international credits that are available from different countries. There are no credits available or loan programs from international financial agencies, and we have seen a great slowing down in G-7 countries or other trading countries' willingness to extend trading credits. But they haven't stopped completely.

I think that the additional measures now that the President is about to sign an Executive Order will strengthen our hand in persuading them that stronger measures on their part are also required.

Mrs. MEYERS. In addition to the sale from Russia, and I think a short time ago there was a sale from China that we had some

concern about, what sort of equipment is India selling to Iran? Do we have concerns about other countries?

Mr. PELLETREAU. Not in the nuclear field. The Chinese contract has not yet been concluded. All parts of the Russian contract have not yet been concluded. We are weighing in just as strongly as we can to persuade those countries not to go forward and continue with that kind of cooperation. And certainly we would do the same with any other country that we saw was showing any interest in providing such technology or equipment to Iran.

Mrs. MEYERS. What industries are going to be most affected in this country by this blockade? I would assume some oil companies.

Mr. PELLETREAU. Well, the oil companies that have been purchasing Iranian oil not for import into the United States but for resale in the international market will be affected.

Mrs. MEYERS. What about agricultural products?

Mr. PELLETREAU. Foodstuffs is certainly one of the exports that is a component of the \$326 million of trade last year. Foodstuffs, auto parts, equipment parts, oil drilling equipment, oil field equipment are all part of—

Mrs. MEYERS. I just think you named everything that comes out of Kansas. I am sorry.

Mr. ROTH. I thank the gentlelady for her questions.

Let me just say that I am constrained to follow up on that by saying that this administration has taken a very, very big step. You have declared economic war on Iran. The Secretary of State isn't even here before Congress. He is going around now trying to persuade other countries to follow in step. Many of us in Congress don't believe in the policy. You have a vote on the floor and I will bet you wouldn't win. So the Secretary of State should be up here selling his program to the Congress because the Congress knows that the only people who are going to lose are your administration and American businesses, which are owed \$400 million by Iran. They are not going to pay the American companies now. The White House said yesterday we are going to lose thousands of American jobs.

The only people we are hurting are our own people and the people who are going to benefit are our allies overseas. The policy doesn't make sense. It is very poorly thought through. I am sorry to have to say that, but I think this is a time when we have to say it.

This reminds me a lot of Vietnam. There is no designated hit, there is neither rhyme nor reason to this thing. This hasn't been thought out. You haven't even talked to our allies. Now we are going to go talk to them. No one is going to follow an uncertain trumpet—and, boy, no one can hear this trumpet.

I would like to yield to my colleague Mr. Rohrabacher. He wants 30 seconds.

Mr. ROHRABACHER. Mr. Chairman, just to put this in context, by the way, if we felt that this policy was being carried out in a very serious way and looked like it was a major effort by the regime, a total commitment by this administration, I think the Chairman would agree with me that Congress could be in support of that because the goal itself, which is counteracting terrorism in Iran and

making sure the Iranians don't get their hands on nuclear weapons, is itself a positive goal.

In context, I would just like to say we have had a lot of discussions here over the last 3 or 4 months about the new supposedly Republican approach to foreign policy, which is more focused on unilateral action and bilateral action rather than multilateral and international approaches. We heard one of our colleagues just talk about the United Nations, and let's just note for the record that we are not getting much cooperation from our friends here, so all of these people are talking about, Let's rely on multilateral actions all of the time. Our friends aren't coming through for us.

You yourself say it doesn't appear that the United Nations, that that is a good way to approach this. We don't have any approach through there now. We have one of our colleagues saying how important it is in talking to our Chairman about the United Nations.

And this is my question to you. Considering the fact that what I just—the litany of details I just went through, and considering the fact that earlier when my colleague, Mr. Gejdenson talked about the United Nations and how we might want to work with the United Nations in confronting this threat down the road, and considering the fact that you verified that within 10 years unless we do something that Iran will have a nuclear-armed missile, is there any possibility that the administration might rethink their opposition to developing a defensive weapons system so we could knock nuclear-armed missiles out of the sky when we were confronted with them 10 years down the road and Iran may not be the only country in the world threatening us?

Mr. PELLETREAU. The answer that I would give you would be, first, that it is not a sure thing, but it is possible—that Iran could have nuclear weapons in that timeframe. And I take the rest of your—

Mr. ROHRABACHER. Well, if it is possible that Iran and countries like that 10 years down the road will have nuclear weapons and have missile technology, I hope and I pray that our colleagues who are all gone on the other side of the aisle now will begin to pay attention to why the Republicans want to build a system that will protect us against that particular threat. It is not pie in the sky, it is not throwing money away, but if that happens 10 years down the road, which you have just suggested it might, it will be comforting, I think, to our people to know that when they start rattling their missiles, that we might be able to shoot them down before they get to New York City.

Thank you very much.

Mr. ROTH. Thank you, Mr. Rohrabacher.

Chairman Meyers, you were going to say something. I didn't want to cut you off, but we have five very important witnesses yet that we want to hear from.

Mrs. MEYERS. Can I ask one more question as a follow-up to what Mr. Rohrabacher was saying?

I can remember that when we were in the middle of Desert Storm we had anticipated that Iraq was some 5 to 7 years away, I think, from having nuclear weapons and missiles, and then we judged that much closer than we had anticipated and thought that perhaps within 2 to 3 years they would have had a nuclear bomb.

Now, how good is our intelligence on Iran?

Mr. PELLETREAU. Well, it has become better since those days and they are very much in mind, the example of Iraq, when Iraq proved to be closer than intelligence estimates at the time thought.

Mr. ROTH. Okay, thank you. Thank you very much, Secretary Pelletreau, for being with us today.

Mr. PELLETREAU. Thank you.

Mr. ROTH. Before moving to our panel of experts, without objection I will now introduce into the record a letter sent to the President from Mr. Michael Armstrong, who is Chairman of the President's Export Council, and top outside committee advising the President on trade policy. Members of the committee have a copy of this letter, and it is a very important letter.

[The letter of Mr. Armstrong appears in the appendix.]

Mr. ROTH. To facilitate the discussion in a logical order, I would like to ask our five expert witnesses to come to the table and present their statements in the following order. Mr. Schott, Mr. Downey and Mr. Lichtblau will present their views of the use of sanctions and their impact on the United States. And then we will hear from Mr. Kemp and Mr. Clawson to discuss how sanctions will affect Iran.

I want to thank our witnesses. I know you have come a long way and you have waited a long time. This is a very important hearing. This is an issue that we in the Congress are going to have to follow very closely. It is going to have a tremendous impact on our country. So I want you to know I very much appreciate you being here today.

Mr. Lichtblau is also accompanied by Mr. Lawrence Goldstein. We are glad to have you with us, Mr. Goldstein.

Jeffrey Schott is a senior fellow at the Institute of International Economics. He is one of the leading national experts on the use and misuse of economic sanctions.

Mr. Schott, would you please give us your testimony.

STATEMENTS OF JEFFREY J. SCHOTT, SENIOR FELLOW, INSTITUTE FOR INTERNATIONAL ECONOMICS

Mr. SCHOTT. Thank you very much, Mr. Chairman.

I welcome the opportunity to comment on the proposed expansion of economic sanctions against Iran. My comments draw heavily on the comprehensive analysis of the use of sanctions that was compiled at the Institute for International Economics in two volumes. This analysis was born in part out of my own frustration working in the U.S. Government in the 1970s and 1980s with the formulation and implementation of sanctions policies against the Soviet Union, Iran, and Libya.

In the interest of time, I will give you a thumbnail sketch of the basic conclusions of the study. Contrary to conventional wisdom, sanctions can contribute to the successful achievement of foreign policy goals, but only under very narrowly defined conditions. Those conditions, when sanctions have been most effective, include: when they have been directed toward a limited and narrowly defined policy goal (the more ambitious the objective, the less likely the sanctions will be effective); when the United States held substantial economic leverage over the target country; when U.S. rela-

tions with the target country had been friendly in the past (such countries are more likely to comply with U.S. demands in deference to the overall relationship, so it is better to hit our friends than our adversaries); when the target country faced economic problems at home and domestic political turmoil; and importantly when the costs to U.S. industries affected by the sanctions were not very large—because such costs inevitably lead to more domestic opposition to the policy and tend to unravel domestic political support for the sanctions over time.

If these conditions are met, U.S. sanctions can be effective unilaterally, and they need not be supported internationally. Unfortunately, as has been already discussed this afternoon, in the case of Iran most of these conditions are not met.

I think it is important to note that the objectives of U.S. sanctions are praiseworthy and they deserve greater international support than they are evidently receiving. But I am skeptical that unilateral U.S. economic sanctions will promote significant reform of Iranian policies.

The sanctions have too little bite, have little support among other countries and may well cause frictions with our G-7 allies, and are likely to be offset by a brigade of what I call Black Knights—countries that are willing and able to provide arms and nuclear technologies to Iran such as Russia and China.

Now, will the unilateral sanctions bite? The answer is not much. Our existing trade relations, as you have noted, are minimal. Direct U.S. exports have averaged about \$550 million a year over the past three years, and account for less than 4 percent of total Iranian imports. The proposals would cut off almost all of those exports; such action would cost U.S. companies a substantial amount of sales to Iran, but would cost Iran very little, since most of those products can be purchased from other foreign suppliers.

I am also skeptical that unilateral sanctions can significantly reduce current and potential Iranian oil revenue. That is because the extraterritorial application of the U.S. sanctions, that block purchases of Iranian oil by foreign subsidiaries of U.S. oil companies, would not decrease Iranian exports since the distribution of those shipments could be easily handled by non U.S. companies. Indeed, as this crisis has percolated, world oil prices have increased and Iranian revenues have increased.

So far, at least, Iran has been a net gainer on the revenue side. Sanctions would reduce Iranian revenues by only a small fraction of the amount generated by the higher world oil prices.

Now, there has been a lot already said about the extraterritorial application of these sanctions. I support the comments of Secretary Pelletreau. The broad application of U.S. sanctions to foreign subsidiaries of U.S. companies would actually have a perverse effect. It would undercut our efforts to build a multilateral consensus in favor of expanding sanctions against Iran because it would distract attention away from the target, and there would be legal disputes, just as there was when we had similar actions during the Soviet gas pipeline sanctions in the early 1980s. In that case, the Soviet Union became an afterthought and we ended up fighting with Europe in the courts and elsewhere about who the real targets of our sanctions were.

I think if such action needs to be taken, or is taken, it would be preferable to limit extraterritorial application to the distribution of crude oil in order to narrow the scope of potential conflict with our allies, but it would have been better if the President had just jawboned the oil companies if he felt it was necessary to get out of the Iranian market, just as President Reagan did in Libya in 1981.

Now, a similar argument applies to proposals to enact a secondary embargo, blocking access to the U.S. market for firms that do business with Iran. I think a secondary embargo would likely violate our international trade obligations when imposed against trade from member countries of the World Trade Organization, and that includes the Europeans. It would exacerbate tensions between the United States and our allies and thus greatly diminish prospects for multilateral action against Iran.

I was a former U.S. trade negotiator. I have written extensively on the GATT. I think I know the GATT very well, and I must disagree with the conclusions drawn by Representative King that a secondary embargo would be consistent under the GATT. I think we would be taken to the GATT and found in violation by our European allies.

Now, that leads to the question of why haven't the Europeans joined us in the sanctions, and I think there has been a lot of confusion about this point in the debate so far. In my view, European and Japanese reluctance to join in expanded sanctions probably reflects both their belief that sanctions alone won't influence Iran's leaders and their unwillingness to risk an escalation of the sanctions in the form of increased political and military pressure.

Remember, the Europeans are much more vulnerable to disruptions of the supply of oil through the Gulf than the United States. They have also been the host to a lot of Iranian terrorist adventures, and so I think it is more the point that the Europeans do not want to rock the boat for fear of the disruption that would befall them. That is the type of concern that has to be addressed if the United States is going to win the support of the Europeans.

I dismiss as extremely naive the claim that European opposition to the less than total U.S. embargo that existed previously reflects doubts about our commitment to counter Iranian transgressions. I think that is just smoke and mirrors, and the real interest of Europe resides in their vulnerability to disruptions of oil out of the Gulf.

I think on that somber note, sir, I will end my oral statement. Thank you.

[The statement of Mr. Schott appears in the appendix.]

Mr. ROTH. Well, thank you very much, Mr. Schott. I know you have given a good deal of thought and time to this issue. We are pleased you have come before our committee today. I think what we are going to do is ask our other panelists for their statements before we go on to the questions.

Arthur Downey is a vice president of Baker Hughes Corporation, an oil service company. Earlier in his career Mr. Downey worked for the National Security Council under Dr. Kissinger, and he is here today representing the National Foreign Trade Council.

And, Mr. Downey, please proceed.

**STATEMENT OF ARTHUR T. DOWNEY, VICE PRESIDENT,
BAKER HUGHES INC., ON BEHALF OF THE NATIONAL FOR-
EIGN TRADE COUNCIL, INC.**

Mr. DOWNEY. Thank you, Mr. Chairman. We very much appreciate your invitation to express the business views and to achieve a balance of views here. I have a very long written statement which is submitted for the record.

Mr. ROTH. We will enter the entire statement, Mr. Downey, into the record.

Mr. DOWNEY. I am pleased also to report that several business organizations, subsequent to the preparation of that testimony, wanted to be associated with it, and I think that emphasizes the unanimity of view within the business community. They are specifically: the Electronics Industries Association, the Petroleum Equipment Suppliers Association, and the American Electronics Association. I will very briefly summarize the long testimony.

Mr. ROTH. Mr. Downey, let me say that I have had a chance to look at your testimony and it is very important, especially for this committee because we also work under the Export Administration Act, and you bring in all the issues, such as extraterritoriality and so on. So it is a good primer for us.

Mr. DOWNEY. Thank you. Indeed, we think the decision tree that is in Section 6 of the Export Administration Act is what should have been followed here.

Mr. Chairman, the issue on the table is not the goals that we are all here discussing, but the method: How can the United States most effectively achieve these goals? And that answer entails weighing costs and benefits and looking realistically at the world around us.

We endorse Dr. Schott's comments about the ineffectiveness of unilateral embargoes. The evidence is overwhelming that they simply do not work. I would suggest that if there is any doubt on the part of anybody on the committee with respect to the impotence of unilateral embargoes, that the committee encourage the GAO or any other respected independent body to investigate and report back before you enact any legislation to that end.

We also agree with Dr. Schott's comments and those of others on the troublesome nature of extraterritoriality. Let me just add a spin on it that hasn't been mentioned, and that is: it is important that you look, that you understand, the awkward position that American-owned companies overseas are put in when extraterritoriality is put into our law, because our closest friends, the Canadians, the British, et cetera, have blocking laws. That means that an American company in Ottawa or in London has to decide whether it should violate U.S. law or violate British law. That is not fair by any account.

What are the costs? What are the costs to the kind of broad unilateral embargo that Mr. King spoke of earlier? We believe they are too high, and, indeed, when you have no benefit resulting from an action, any cost is too high. There is the loss of direct exports from the United States. It is not a great deal, a little over \$300 million. That is a drop in our bucket. But nevertheless those exports do support jobs, and they do support jobs, as you indicated earlier,

from frozen chickens and auto parts, and oil field equipment and rice and soybean oils.

You alluded in your opening remarks to the issue of debt. This is normal, routine international trade debt owed to American companies by Iran for products and services already provided. This is not broad, untied financing of infrastructure projects, and, as you indicated, you can be absolutely certain the Iranians are not going to pay those debts.

Who suffers? Not the Iranians. They are going to have more cash than they otherwise would have, by not having to pay down the American debts. The losers will be the American companies who will not get paid. You then have an ironic result: The actions of the U.S. Government will result in Iran receiving free American products at the expense of American companies.

We have heard, and you noted the problem, when you have a unilateral embargo of this type where America's customers have firmed up in their mind that American companies are not reliable suppliers. That means that every day, with increasing frequency as this goes on, foreign companies who are potential buyers of American products design out American products.

There is also an impact, a beneficial impact, on our foreign competitors. Just let me give you one hypothetical. Put yourself in the shoes of a small French oil field safety equipment manufacturer that has had a real hard time trying to break into the Iranian market or Middle East market. Now, with the Americans out of that market, the French can go in and substantially increase their profit margins because the U.S. competition is gone. That also means that this hypothetical French company can use its excess profits to subsidize its prices in other markets to compete with American companies there.

The irony, again, is overwhelming. The U.S. Government would be assisting foreigners to compete better against American companies in the global market.

Therefore, for all these reasons, it becomes apparent why no American company complains about the embargo against Iraq, despite its costs, because in the case of Iraq the embargo has been effective. It is not extraterritorial, and it is multilateral. All companies, U.S. and non-U.S., share the burden. All competitors bear the same burden, and U.S. companies are not singled out nor branded as unreliable.

Are there alternatives? Yes. Clearly, if the threat from Iran is so deadly serious, presumably covert action should be employed. If Iran is a democracy, however primitive and however corrupt, unlike the dictatorship in Iraq, wouldn't massive doses of information and engagement ultimately force a change in behavior? I suspect that the regime there would be more threatened by broadcast of CNN or MTV than by not being able to buy American frozen chickens.

The National Foreign Trade Council presented the Administration with a specific and detailed proposal for economic sanctions—we recognize they have a place—highly targeted on matters relating to terrorism and weapons of mass destruction. We haven't had a response.

Let me make a note on the fact, I think the Chairman alluded before to the Export Administration Act, that the President's action will be under the International Economic Emergency Powers Act, which we would encourage you to review later in this Congress. It has become sort of the Bay of Tonkin Resolution for international economic issues. It is an overbroad grant of authority to the President, and we believe the Congress should return some of that authority to where the Constitution originally put it.

Concluding, a broad unilateral embargo will result in the equivalent of \$1 billion tax over time levied only on American companies, a tax, however, where the proceeds flow not to the U.S. Treasury, but flow to American competitors overseas.

A final comment, Mr. Chairman, on the Executive Order that we anticipate any moment. I read very carefully the President's speech in New York and Secretary Christopher's statement yesterday. The proposition seems to be that this total unilateral ban will enhance the credibility of the United States, so that there will be increased hope that the United States can persuade its allies to suspend or reduce subsidized credits to Iran. That is the logic.

Daniel Schorr said on NPR last night the administration's logic was flabby. I think he was chartiable. This "bold" decision by the President—as we heard all afternoon how bold it was—"underscores America's readiness to lead by example."

I remind you, however, the United States does not subsidize credits for Iran and hasn't for 15 years. Where is the credibility? The United States has not imported Iranian oil since 1987. Isn't that sufficient credibility?

Why is it necessary for the United States to impose a total ban on all transactions just in order to increase the possibility that our allies might reduce their subsidized credits?

Sure, the President's action will make it marginally easier for diplomats, but I wish in the future the United States would draw down its diplomatic capital, rather than draw down the competitiveness of U.S. companies. While we believe there is no chance—no chance—that the allies will match this embargo, we would urge you not to legislate.

Give the President a chance. We hope he is right. We would applaud that, in multilateralizing the sanctions. But if the administration fails, as we think it will, to multilateralize the sanctions in three months, four months, five months, we would urge you to pressure the President to remove this unilateral ban. It is hurting our competitiveness long term.

Thank you.

[The statement of Mr. Downey appears in the appendix.]

Mr. ROHRBACHER [presiding]. Thank you very much, Mr. Downey.

As you can see, I am in the Chairman's seat, so things have really changed.

Let me just note, I appreciate that both of our witnesses so far are really not taking the administration to task about the goals that it has in mind in terms of influencing the policy in Tehran, but you are certainly suggesting that the methodology is somewhat flawed. So I would like to now call on Mr. Lichtblau, and he is Chairman of the Petroleum Research Foundation.

We appreciate you coming all the way down here from New York to be with us today. Thank you very much.

**STATEMENT OF JOHN H. LICHTBLAU, CHAIRMAN,
PETROLEUM INDUSTRY RESEARCH FOUNDATION, INC.**

Mr. LICHTBLAU. Mr. Chairman, our testimony was submitted to your committee last Friday. Thus it does not contain any reference to the pending Presidential order which was issued on Sunday.

I believe that this order, together with the one issued last March on U.S. investment in Iran, completes the new U.S. policy on Iran, and it is possible that this latest Executive Order, together with the one issued previously, could obviate any congressional action at this time since both have the same goal; namely, to prohibit any trade with Iran, and any U.S. investment in Iran. The question, however, is whether the measures proposed in H.R. 1033 or in the new Executive Order will actually hurt or threaten to hurt Iran enough to bring about a change in its policies.

I would like to go briefly through the various aspects of the proposed legislation to analyze this question. Let us first look at the investment aspect of H.R. 1033. The investment restrictions in the bill have largely been addressed through the Executive Order of March 15, 1995, which prohibits all forms of U.S. investments in Iran. It was prodded by the congressional focus on Iran and the proposed billion-dollar Conoco oil field development contract with the National Iranian Oil Company.

In the short run, cancellation of the Conoco contract will hurt Iran. In the long run, the readiness of non-U.S. companies to invest in Iran will become clear. At least two European companies have already been reported as negotiating, and several countries, as we have heard earlier, have just declared they will not follow U.S. policy on Iran.

Thus, the White House Executive Order in the Conoco situation can be assumed to have some limited negative impact on the Iranian oil sector both in delaying any non-U.S. contracts and in making the terms less attractive for Iran than the canceled Conoco contract.

The negative impact, however, will be fleeting. Geologically and economically, Iran is one of the world's most attractive oil investment areas. Iran's current productive capacity is 3.6, 3.7 million barrels a day. In the five years prior to the Iranian revolution in 1979, it was five and a half to six million barrels a day. The decline is not due to a declining resource base but to a combination of neglect, war damage, and lack of funds to rebuild its capacity.

Since virtually all forecasts agree that all Persian Gulf producers must increase their output substantially to meet world demand, foreign investment in the Iranian oil sector will be both attractive and necessary. In the absence of U.S. companies, European oil companies can be expected to undertake these investments, regardless of U.S. policy.

My next point is the proposed total ban in H.R. 1033 on all Iranian oil liftings by U.S. companies and their foreign affiliates. Iran exports about 2.6 million barrels of oil a day. Europe takes about half of this total and about a million barrels go to Asia, most of which goes to Japan. Some 600,000-650,000 barrels a day of these

exports, worth about three and a half to four billion, were purchased by a number of U.S. companies in 1994 outside the United States.

There is no doubt that if Iran lost these 600,000 barrels a day of exports, its economy would be weakened. However, the implied assumption that if U.S. companies could no longer purchase these volumes, Iran's oil export volume and value would decline substantially is not borne out by the facts, in our view.

The reason is the same that caused Iran very little harm following the reinstatement of the U.S. import embargo in October 1987. No other country joined the U.S. embargo, and a unilateral trade embargo of a globally traded fungible commodity is by definition ineffective.

There is currently no indication that any oil importing country has any intention to change its position on Iranian oil imports. Thus, while passage of H.R. 1033 might cause a very short-term dislocation for the 25 percent of Iran's oil exports bought by U.S. companies, the world oil market would quickly redistribute Iranian oil to other markets and customers to restore any temporary imbalance.

Now, I would like to talk briefly about Senate Bill S. 630. Senator D'Amato has recognized the possibility that foreign companies may offset any negative impact on Iran of a global embargo in the Iranian oil purchase by U.S. companies and has therefore introduced S. 630. In the Senator's words, "A foreign corporation or person will have to choose between trade with the United States or trade with Iran."

S. 630 goes far beyond preventing foreign companies from buying the Iranian oil that U.S. companies will be forced to leave behind under H.R. 1033. It would force foreign companies or individuals who want to do business with the U.S. to cease buying any oil or any other commodity from Iran. The same would apply to exports to Iran.

There is virtually no chance that the U.S.'s foreign trading partners would accept this form of secondary trade boycott. They could be expected to protest, then retaliate.

But should we even want to see all or most Iranian oil exports eliminated? From an economic point of view, the answer is clearly no, under current conditions. Iran accounts for about 7½ percent of total world oil exports. If all or most of these exports became unavailable, the price of oil would rise substantially because the world market would have insufficient supplies at current prices.

The world's current excess producing capacity amounts to about 3 million barrels a day, of which 2 million barrels a day is located in Saudi Arabia. Suppose our policies succeeded in reducing Iranian oil exports by 50 percent or 1.3 million barrels a day. Under current conditions, that is continuing full U.N. sanctions on Iraqi oil exports, this would reduce available world oil exports by nearly 4 percent and would result in a price increase of perhaps \$4 a barrel or the equivalent of 10 cents a gallon.

Thus, the advocates of global restrictions on oil imports from Iran beyond the elimination of U.S. companies' purchase of Iranian oil are faced with sort of a Catch-22 situation. The more they succeed in their endeavor to cut the Iranian exports, the more the

price of oil will rise, with attendant negative impacts on the economies of all importing countries, including the U.S. For the moment, this is the reality of the oil market.

Finally, let us examine what the proposed embargo would do to U.S. companies currently engaged in the Iranian oil trade. In the broader sense it would be a mirror image of the bill's impact on Iran. The affected U.S. companies would have to switch to a non-Iranian supply source for approximately 600,000 barrels a day. Over time, they would be able to do so.

The U.S. oil companies, however, would not be indifferent to being denied all commercial access to Iran, currently the world's second largest exporter, while their foreign competitors maintain unrestricted access.

As I said at the beginning of my testimony, there may well be overriding noneconomic reasons for the U.S. to prohibit U.S. companies from doing business with Iran. However, as long as other countries do not actively support our policy, the impact of H.R. 1033 on the Iranian economy will be marginal at best and short-lived. So, American companies are likely to be more affected by H.R. 1033 than its intended target, the Iranian economy. Thank you very much.

[The statement of Mr. Lichtblau appears in the appendix.]

Mr. ROTH. Thank you very much, Mr. Lichtblau. We very much appreciate your testimony. You have a good deal of background and we in Congress take very seriously what you, and this panel, are saying and have said.

Geoffrey Kemp is a senior associate with the Carnegie Endowment for International Peace. He is the author of several books on the Middle East, most recently, "Forever Enemies? U.S. Policy and the Islamic Republic of Iran."

Mr. Kemp, please proceed.

STATEMENT OF GEOFFREY KEMP, SENIOR ASSOCIATE, CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE

Mr. KEMP. There is increasing consensus between the United States, several of its European allies, Japan, Israel, and many Arab countries that Iran behaves in ways that are inimical to Western interests. Of particular concern is Iran's putative nuclear and missile program, its conventional military modernization program that could challenge U.S. maritime supremacy in the Gulf and its adjacent waters, and its avid opposition to the Arab-Israeli peace process, including support for radicals and terrorists intent upon destroying the Israeli/Palestinian accords.

Of these concerns, Mr. Chairman, Iran's nuclear ambitions are by far the most serious and warrant priority action to be taken jointly with our key allies. The wisdom of new sanctions should be measured against this primary yardstick: Will they reduce the probability that Iran will obtain nuclear weapons in the next 10 years or so?

The current debate in Washington is not therefore about the nature of Iranian behavior. There is consensus that it is unacceptable. It is about the costs and benefits to U.S. interests of imposing increased sanctions against Iran, including greater restrictions on trade and penalties against foreign governments and companies

that sell Iran strategic items that can assist in its weapons of mass destruction programs and its overall economic well-being.

The administration has, as we have heard, enunciated a policy of dual containment for confronting both Iran and Iraq. Now, this policy includes military strategies designed to deter and, if necessary, defeat any Iraqi or Iranian military aggression in the Gulf.

Since the Gulf war, U.S. military cooperation with Arab allies in the GCC has grown, and the forces we have earmarked for possible intervention are well equipped and prepared for most short-term contingencies. The administration has also orchestrated a political and economic campaign to continue U.N. sanctions against Iraq and to try to isolate and weaken Iran. While Iran is not, of course, subject to U.N. sanctions, the U.S. is trying to pressure the Islamic regime to change its ways.

This latter policy has only been partially successful, and we have been roundly criticized for continuing a flourishing economic relationship with Iran while calling on allies to reduce their own commerce with the regime. This explains in part why President Clinton announced on April 30 that he would sign an Executive order essentially ending all U.S. trade with Iran. A related reason for this action is the administration's hope that it will preempt much more draconian measures proposed by the Congress, in particular a draft bill submitted by Senator D'Amato.

Both administration and congressional efforts to impose more sanctions against Iran must be examined in the context of costs and benefits to American and Iranian interests. The U.S. must also assess the likely reaction of Iran's key economic partners, such as Germany and Japan, and of Iran's key suppliers of military technology, especially Russia, China, and North Korea.

It is essential that the long-term implications of proposed sanctions legislation be widely debated. Given the current universal antagonism toward Iran in the United States, it would be easy to pass laws that seem tough now, but could eventually rebound to our disfavor.

Will increased sanctions weaken the Islamic regime to the point where its leaders will adopt more moderate policies, or will they make the leaders more defiant and dangerous? Will our allies take seriously new congressional legislation, or will they ignore our homilies and continue business as usual? How will U.S. economic interests be affected? In this testimony, I focus on the first two questions, which are of a more political nature.

Some would use the example of Iraq to suggest that desperate regimes do desperate things. They would argue that it was economic desperation that led Saddam Hussein to use his considerable military assets against Kuwait in August, 1990.

I think we all know that had he used his military assets in a more Machiavellian manner, he could have achieved his goals without embarking on a war with the rest of the world. Iran, it could be argued, may find itself in a similar predicament if sanctions are tightened and its economy continues to deteriorate.

A desperate regime dominated by radicals could use its limited military assets not to invade a neighbor—the Iranians simply do not have the assets to do that—but to change the nature of politics and confrontation in the Gulf. Some, particularly those across the

river in the Department of Defense, have postulated that Iranian submarines or aircraft could lay mines in shipping lanes or use shore-based missiles to attack tankers and try to block the Straits of Hormuz.

The purpose of such actions would not be to achieve any maritime victory over the United States, but rather to sow panic through the oil markets and to put the Arab Gulf on notice that Iran will not sit back and allow its revolution to be squashed.

In such circumstances, the United States' military assets are adequate to ultimately defeat any Iranian military action, although whether a limited engagement would in this context be in America's interest is another matter. On the other hand, escalation to a full-scale war with Iran would pose an enormous set of problems for the United States, both militarily and politically. These types of threats could evolve in the coming months or years, if those who believe that the Iranians will strike out when cornered are correct.

Now, of course, there are those who hold that if Iran is in dire economic straits, it now has to be careful about further isolating itself from the rest of the world, as it would do by interfering with oil traffic. Rather, it will have to reach out and make compromises, not necessarily with us or with the West, but with its neighbors. It might do this to avoid a domestic implosion, which could be triggered by economic deprivation and social unrest, of which there is considerable evidence existing today in Iran.

Advocates of this view would point to Iran's relations with Russia, with the Caucasus, and with Central and South Asia—for instance, the recent trip through India by President Rafsanjani—to show that this regime is quite capable of being very pragmatic and nationalist in its foreign policy when dealing with its neighbors to the North and to the East.

Nevertheless, the most persuasive political argument for tighter restrictions on U.S. exports to Iran and on the purchase of Iranian oil by U.S. oil companies is that unless the United States is prepared to make economic sacrifices to implement its policy of containment, it has little moral authority to ask others to deny themselves access to the Iranian market.

It has been difficult to convince allies of our seriousness so long as we remain one of Iran's key trading partners and our oil companies buy billions of dollars of Iranian oil. Stopping U.S. oil companies from doing business with Iran may not initially change Iranian behavior, but it certainly makes it easier for the U.S. Government to demonstrate its resolve. However, Mr. Chairman, this approach alone will be insufficient to persuade our allies and our friends to tighten economic pressures on Iran. And this brings us really to the key question of the linkage with the nuclear issue.

The most compelling case to be made for tougher sanctions against Iran concerns its activities with respect to nuclear and missile development. There are two routes Iran can follow to get the bomb. First, by openly proceeding with its civil nuclear program with the cooperation of Russia and China, Iran will develop a nuclear infrastructure and a trained cadre of engineers and scientists. There experts will be familiar enough with the process to make it possible for Iran to move toward a nuclear weapons program were

it ever to formally withdraw from the Nonproliferation Treaty, which it is legally permitted to do.

The second route to nuclear weapons, the covert route, would be for Iran to cheat on its NPT commitments and go ahead with efforts to jump-start a nuclear program, using technology and support procured from the black market. This route would undoubtedly shorten the time needed for Iran to get the bomb, but Iran would risk being discovered and triggering economic sanctions not just from the United States, Europe, and Japan, but from the United Nations as well.

The preferred American policy must be to orchestrate and sustain multilateral containment of Iran. The more conclusive the evidence that Iran is undertaking a serious nuclear weapons program in violation of its NPT commitments, the easier it will be to persuade the allies, especially the West Europeans and Japan, that business as usual with Teheran has no impact on moderating Iranian behavior in this most critical arena. We should remember that the Europeans and Japanese have often argued that if we do business with this regime, it will moderate, and it has not worked.

There is evidence that our overtures to date have already begun to have some impact on Britain, France, and Japan. Additional homilies concerning Iran's appalling human rights record, its support of terrorism, and its opposition to the peace process, while important, are likely to be less persuasive.

Japan, for instance, now seems to be having second thoughts about the help it is offering Iran with huge hydroelectric programs. In my judgment, convincing Germany to change its policy toward trade with Iran will be more difficult and remains one of highest priorities.

Convincing the Russians to back down from their avowed intention to sell Iran nuclear reactors and possibly centrifuge technology requires both sticks and carrots. The new legislation proposed by Senators McCain and Lieberman and Congressman Lantos focus on penalties for Russia if it continues with the sales.

The McCain and Lieberman bill would strengthen the existing Iran-Iraq Arms Nonproliferation Act of 1992. The proposed Lantos bill would put Russia on notice that if it proceeds with its nuclear sales program to Iran, it will forfeit further American economic assistance other than that earmarked under Nunn-Lugar to dismantle and control weapons in the former Soviet Union.

Mr. ROTH. Dr. Kemp, although we appreciate your testimony, I wonder if we could ask you to wrap up because we like to go to some questions and when we have the time for questions, we would like to ask the panel some questions.

Mr. KEMP. I have one more sentence then, Mr. Chairman.

But Russia will not back down on this sale unless some carrots are offered, preferably as part of an overall review of U.S.-Russian policy on technology transfers worldwide. Unless some tacit market-sharing agreement is negotiated, the bureaucratic and economic pressures on Russia to conclude legal sales of nuclear and conventional technology will continue.

Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Kemp appears in the appendix.]

Mr. ROTH. Well, thank you very much, Dr. Kemp, and we appreciate that you have given this a good deal of attention and study and we appreciate your testimony before our committee.

Patrick Clawson is a Senior Fellow at the Pentagon's Institute for National Strategic Studies. He is a leading expert on Iran's activities in developing nuclear weapons and terrorism.

Dr. Clawson, we are going to ask you to proceed.

Mr. CLAWSON. Thank you very much.

Mr. ROTH. We are going to enter your entire testimony into the record.

STATEMENT OF PATRICK CLAWSON, SENIOR FELLOW, INSTITUTE FOR NATIONAL STRATEGIC STUDIES, NATIONAL DEFENSE UNIVERSITY

Mr. CLAWSON. Thank you. Then in the interests of time let me just make a few remarks drawing upon my prepared statement.

I am an old-fashioned sort of person and I have great difficulty understanding whether or not the sanctions against Iran will be successful until I first understand what it is they are intended to succeed at. And therefore, I would like to address the question of what are our goals with respect to Iran, because I think that that would help us to understand whether or not these sanctions will be effective at achieving those goals.

One goal some people have offered with respect to Iran is to destabilize the present regime and indeed to overthrow it. I think it is extremely unlikely that sanctions would accomplish that aim. We do not have the capability in the U.S. Government to affect Iranian domestic policy to that point.

Another suggestion that has been made is that in fact, our aim is to contain Iran. When I hear the word containment, I think of the classic article by George Kennan from 1946 where he suggested with respect to the then Soviet Union that an appropriate policy would be to limit the ability of that country to engage in external aggression and meanwhile wait for its internal economic problems to eventually lead to the implosion of that society, for he was firmly convinced that the Soviet system was not one that could last.

I think that kind of a policy of containment—namely, limiting the regime's ability to engage in external aggression while awaiting for it to fall apart—has good prospects with respect to Iran.

I say that in part because I think the Islamic Republic of Iran is in fact in miserable shape internally. It has not turned out to be a very successful system. It is not lasting very well into a second generation after the death of the charismatic leader, Ayatollah Khomeini, because his claimed uniting of religion and politics isn't really catching hold among the Iranian people. Iran is one of the few countries in the Islamic world where we find that the young are turning away from devout religious behavior more than being attracted to the wave of religiosity that seems to be sweeping the Muslim world.

Furthermore, there is considerable dissatisfaction by the senior clergy with the regime in Iran. They don't like seeing religion relegated to being a department of the government. So I think there is a reasonable prospect to expect that this regime will in fact im-

plode and I think that sanctions can play an important role in weakening the regime by depriving it of foreign exchange.

I am concerned that in some of the comments we have heard today there is really remarkably little knowledge about the situation that Iran has faced in the last 4 years. May I point out, sir, that in 1992 Iran's imports were \$25 billion. That was the year before the Clinton administration came into office. Last year Iran's imports were \$10 billion. Now, I would say anything which reduces Iran's imports by 60 percent in the space of 2 years is a policy which certainly has not been 100 percent effective, but my goodness gracious, I would say there is something there that has had an effect.

Going from \$25 billion in 1992 to \$10 billion in 1994 has had something to do with the fact that the U.S. Government has been in a vigorous campaign to prevent Iran's normal access to international capital markets. Iran went from borrowing \$10 billion a year on international capital markets to instead having to repay \$5 billion a year. So while its oil revenue was relatively steady over that period, its imports fell over 60 percent. Now, that is not a fall of 100 percent, but it is something which weakens the regime.

Partly as a result of that, I would say largely as a result of that, Iran had to formally abandon its \$2 billion a year program to import arms and says that it is only able to import \$800 million a year in arms. That is the difference of a couple of submarines, a whole lot of fighter planes, and a whole lot of other nasty stuff as well as a very significant slow-down in what had been a high-speed nuclear program to a relatively low-speed nuclear program. To my mind that makes a difference.

Now, a third suggestion that could be made about what our policy goals are with respect to Iran is the suggestion we usually hear from the administration, which I find rather unconvincing, which is that our goal is to modify Iran's behavior. And as several people have suggested, it seems unlikely that sanctions are going to be particularly effective on that goal of persuading the Islamic Republic to modify its behavior.

I am quite skeptical of the idea that we are, in fact, going to be able to use carrots and sticks in order to be able to persuade the Iranians to temper their behavior and in particular, I don't think any carrots we offer are going to be sufficient to persuade Iran to change its behavior.

Our experience in 1985 to 1986 with the Iran Contra affair when we offered some pretty sweet carrots was we didn't get very much for it and the Europeans didn't get very much with their extensive loans either. And on the stick side, I am also a bit skeptical that we are going to be successful in persuading the Iranian Government to change its behavior.

With that said, I should note that we have had considerable success at getting our allies to join us in applying some of the sticks that we have wanted. And that is when this administration came into office, many of the Western allies were quite wishy-washy on the question of whether or not they would sell weapons to Iran. There is now a wall-to-wall consensus that these countries will not sell weapons to Iran and that is quite well observed. In fact, we

have even gotten the Russian Government to say that it is not going to make new arms deals with Iran.

Furthermore, when this administration came in, there was an awful lot of dillydallying around about dual use. Yet now we find that there is quite vigorous activities by our allies to prevent dual use sales to Iran. May I point out that for instance the last year for which I have data with respect to the U.K. that over one-third of all export license requests to Iran that were filed with the British Government were denied. That is a pretty good turn-down rate.

Furthermore, we find that the German Government has implemented an extraordinarily vigorous program, not completely successful by any means, in order to prevent dual use technologies reaching Iran. Quite a change from its behavior with respect to a number of other countries where we raised issues with the German Government in the past. So I think that there has been some small successes in getting our allies on board. However, that has had very little impact on Iranian behavior. So I am quite skeptical that we, in fact, are going to be successful if our goal is modifying Iranian behavior.

If I may close with a final comment, I am quite skeptical about the argument that we are losing significant business opportunities in Iran. May I suggest that our imports in Iran have already gone down from \$720 million a year in 1992 to \$330 million a year in 1994. That is a pretty impressive drop.

And I think that, in fact, most of what we are hearing today reminds me very much of the kind of debate that we heard in the spring of 1993 with respect to the billion-dollar deal that Boeing had negotiated with Iran. When that deal was effectively "kiboshed" by the new administration, we were told that Airbus and others would step in and have a wonderful market opportunity.

Well, here we are two years later and so far the only thing that Iran Air has been able to do in the last two years is to rent a few used and decrepit Russian planes. They don't have the money to be a significant market and, in fact, what has happened is that Iran as a market is collapsing for reasons that have nothing to do with the new sanctions we imposed and have much more to do with the incompetence of the Iranian Government and with our successes at blocking their access to international capital markets.

[The statement of Mr. Clawson appears in the appendix.]

Mr. ROTH. Thank you, Dr. Clawson, and all the panelists. Again, we appreciate you taking your time being with us today and giving us the benefit of your testimony.

Let me just ask you a couple of questions. Mr. Schott, are you surprised that the EC and France and U.K. and others turned us down flat on this initiative? What could we do to make this embargo work?

Mr. SCHOTT. Well, I am not surprised given the way that the policies have been implemented so far. As I said in my opening statement, I feel that what is really driving European policy when you get rid of all of the window dressing is really their concern and their vulnerability about disruptions in the Gulf.

And one needs to address those security interests. So some of the points made by Dr. Kemp are valid. We need to have a much more

integrated policy that addresses security interests in that region, including the role of Russia and how the Europeans and Russians work together. If we had used leverage on the Europeans regarding their concerns about the development of Russia, I think we could have had more success in getting them to join our efforts to sanction Iran. But it is not an easy task because they run a much bigger short-term risk than we do if this sanctions policy fails and, as has often happened in recent sanctions cases, if the sanctions become a prelude to military action. And I think that is what is driving their reluctance to join us.

Mr. ROTH. Thank you. Dr. Lichtblau, you mentioned, as I understood it from your testimony, that the basic point is Iran's oil production is too important to the global markets to ever be effectively embargoed. And last Friday, I noticed in the paper that the Royal Dutch Shell Company picked up the slack left by the canceled Conoco project. Enlighten us a bit on that. Are you surprised by that?

Mr. LICHTBLAU. No. No. I was sure that some company would pick that up. In fact, at the testimony at the Senate Banking Committee, the witness for Conoco said that President Mitterrand himself had called up the President of Iran Rafsanjani to try to get Total French Oil Company involved in the deal and ended up being turned down and the deal was given to Conoco. It was at that high a level that France wanted to be involved with Iran. And I am not at all surprised that foreign companies go in there.

It is, as I said, a very attractive area and any country that is as rich in oil as Iran has to be counted as an important power because of that. It doesn't mean they can do anything they want to. But to say we can cut off their oil and punish them, this kind of use of oil as an instrument of policy by the consuming countries, which is the opposite of what the producing countries did for a brief period in the 1970's. I don't think it will work.

Mr. ROTH. Do you think that oil companies are going to use this as a pretext for increasing gasoline prices at the pump? In other words, is the American driver going to have to pay more because of this?

Mr. LICHTBLAU. I have a strange idea that oil prices are determined by market forces and if that is correct—

Mr. ROTH. Yes, but they went up 10 cents the other day, the day after the embargo.

Mr. LICHTBLAU. Well, but that is 10 cents a barrel. That is not 10 cents a gallon. That is a tiny fraction. Mr. Goldstein could comment on that.

Mr. ROTH. Well, I was told by the people that work here on Capitol Hill that gas prices went up as much as 10 cents a gallon at the pump.

Mr. LICHTBLAU. Not overnight, I don't think so. If it did, there is a gasoline market tightness at the moment. There is also a question of moving from regular gasoline to reformulated gasoline.

Mr. ROTH. I was just interested in your comment on that issue.

Mr. LICHTBLAU. It has nothing to do with the Iranian situation.

Mr. GOLDSTEIN. If I might, just briefly, the oil markets today are radically different than in the 1980s when you had 8 to 10 million barrels of spare productive capacity on an average basis over that decade. Today you have 3 million barrels of spare capacity, 2 mil-

lion in Saudi Arabia. Therefore an effective embargo on Iran falls into the category of what I would suggest is "be careful what you wish for," because if in fact it was effective and our allies did support us, the entire spare capacity in the world market disappears overnight.

Spot prices would rise, a risk premium for oil prices would probably return to the market, a desire to accumulate inventories at the primary, second, tertiary level would drive prices up further. In that environment, we could see the concern again reawakened for inflation. The Fed Chairman might take another look at its current policy. The prospects of a soft landing would be very much put into question. That is part of the costs of this policy. Economists can't tell you and shouldn't tell you what policy should be, but we can put price tags on those policies.

Mr. ROTH. Thank you. Mr. Rohrabacher, and I appreciate your taking over the Chair when we had a vote here. I would like to ask you for your questions.

Mr. ROHRABACHER. Actually, what you appreciate is that I gave it back.

Mr. Chairman, thank you very much. Coup d'etat, right, while you were out voting. I noticed that Mr. Downey suggested that covert action—he just said that in passing, blah, blah "and covert action," blah, blah.

And would you be supportive of covert action in situations like this? Iran is going to receive—are going to start opening up a—I mean, after all, in Iraq they are opening up a nuclear plant and the Israelis took care of that. It wasn't covert, but they took care of the business.

Mr. DOWNEY. It certainly was not my intent to get beyond my sphere of competence. And covert action is not within my sphere of experience.

Mr. ROHRABACHER. I thought I heard that phrase come out of your mouth.

Mr. DOWNEY. I said it because I said, if the threat is as serious as we hear, then the uneducated would say, gee, fellows, isn't that something you take care of by covert action, among other things. And then we went on to other things, like how about the radios, when it was the Soviet Union we had Radio Liberty, Radio Free Europe and so on.

Mr. ROHRABACHER. That is not your area of expertise, but it might be Dr. Kemp's area of expertise.

Mr. KEMP. Well, yes, I think we have to consider all sorts of policy options if, indeed, Iran is on a nuclear track and we can't get them off it by pleading with them. And certainly I think a whole array of covert operations should be taken into account, most importantly to deter former Russian scientists from going to work for them for rather large fees, but I really do think this is an issue that will be totally ineffective unless it is coordinated with our allies and unless we have a very serious discussion with the Russians.

Now, one of the things I think we have going for us is that the bureaucracy in Moscow is split on this issue. There are those in the Russian foreign ministry and in their policy planning circles who worry just like we do about an Iranian bomb 10 years from now.

The problem is that they have very little leverage over a huge industry that needs to employ people, and I don't believe we can convince them, bring them around to our side, unless we offer them something else instead.

All the Russians see from us is a litany of denials. We deny them rockets to India. We try to cut them out of the East European market, the Southeast Asian market. We don't allow them into the Gulf market. It is no wonder that on these issues they take a very tough line.

Mr. ROHRABACHER. Let me be very specific here because, first of all—about another issue rather than just the nuclear development of a nuclear device. If indeed the Iranian Government is involved in the massive printing and distribution of U.S. currency, would we be justified in blowing up that printing press?

Mr. KEMP. Yes.

Mr. ROHRABACHER. Number two, if the nuclear—by the way, I think that is a very good answer and thank you very much. And who is to do it, that is all right. In terms of if diplomatically and economically we fail in thwarting efforts by the Iranians to obtain the technology they need to produce a nuclear weapon, would you think that a covert operation to, for example, someone accidentally tosses technology off a ship or outside of an airplane door, something like that, is that the type of covert action that would be—

Mr. KEMP. These are types of little plans that I think—I hope, are being discussed as we speak. However they should not be discussed in any more detail in this room, since I think they are a good idea.

Mr. ROHRABACHER. Okay. Mr. Kemp, I would suggest that we should—and I know the title of your book is that we are in this hate relationship with the Iranian Republic, with the Islamic Republic in Iran. I would hope that the leaders of that regime understand that the people of the United States—again, let me repeat, the people of the United States want to be friends with Iran. There is nothing but good things for all of us by being friends.

This is so ridiculous that we are sitting here talking about possible covert operations, all of these things, the economic tactics that are going to hurt our countries with a government and a group of people who have no real conflict with the United States other than some ideological concept.

So I would hope that the people of Iran, who I do not believe want to have a hate relationship with the United States, I hope they take my comments to heart because I think that they will—I hope they hear them because we want goodwill and peace and prosperity and we don't want to waste our money and our lives on things such as this. And I thank you all very much for all that great testimony and I appreciate it, Mr. Chairman.

Mr. ROTH. Well, thank you very much, Mr. Rohrabacher. I join my friend, who is one of the most knowledgeable people in the Congress, on what is taking place because he has been able to visit many of these countries. I don't have a chance to visit many of the countries because I am so busy here in this country, unfortunately, but I hear from my friends that are overseas during the break and they said it is nothing but corruption in Eastern European coun-

tries. There is no government. The Mafia is involved and everything.

You know, Mr. Clawson, you had mentioned before about what is happening in Iran and I think, Mr. Goldstein, you said you ought to be careful what you pray for, for your prayers may be answered.

Suppose the government does fall in Iran. What kind of government are we going to have in Iran? I mean, you are working at the Pentagon, maybe you could enlighten us.

Mr. CLAWSON. Let me emphasize my views here are purely my own. I am not by any means representing the Department of Defense here. Iranians are tired of ideology and that is one of the reasons why they dislike the current regime. I think it is highly likely that if the present regime in Iran were to be replaced by another, it would be replaced by a regime which is not intensely ideologically motivated, which is seen as being nationalistic, competent—

Mr. ROTH. Like the Shah maybe, but evidently he didn't last.

Mr. CLAWSON. And also, frankly, he was always seen as being more interested in feathering the nest of his family and friends than he was in caring about the Iranian people. So I suspect that the Iranians would want somebody who is seen as more interested in the day-to-day welfare of ordinary Iranians, I think the one thing we can be reasonably sure of is that whoever replaces in the Islamic Republic is not going to be interested in any ideological crusades like opposing the Arab-Israeli peace process, an issue which is far removed from the national interests of Iran where I think relatively few Iranians care about this and where the Iranians manage to really annoy the United States without getting very much for themselves.

Mr. ROTH. Well, I very much appreciate your testimony and it is very important, what we are doing today. I really feel that when we say the old world is gone, I really believe that. I don't think that we are going to see wars in the future, but we are going to see tremendous economic wars and I think that this is an indication of it again today when we talk about these embargoes.

I believe that what the administration is trying to do in the end is good. We want to keep nuclear weapons out of the hands of these pariah regimes. I think how we go about that is very important. With the huge trade deficit that we have, with the jobs our people need, I think we have got to look at these things with more perspective and more circumspection.

When the administration comes to us and says, "we just put on an embargo" and what do the French say? "Sorry." The Germans? "So what, we haven't". I sit back and say, hey, am I on the same planet with the State Department? Sometimes I am afraid I hear more insight in the taverns in Wisconsin than I do in the White House and that scares me. So I am concerned and I am glad to have your expert testimony here and I hope that we can call on you

in the upcoming weeks and months because this is going to be an ongoing problem I am sure. Thank you very much, gentlemen.
[Whereupon, at 4:34 p.m., the subcommittee was adjourned.]

APPENDIX

PETER T. KING
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STATEMENT OF
REPRESENTATIVE PETER T. KING (NY-3)
SUBCOMMITTEE ON
INTERNATIONAL TRADE AND ECONOMIC POLICY
MAY 2, 1995

Mr. Chairman, I greatly appreciate the opportunity to testify here today on the absolute necessity of the United States adopting strong, air-tight and unambiguous sanctions against the outlaw regime in Iran.

Mr. Chairman, I know it is your style to cut through the formalities and get right to the basics and that's what I intend to do.

Iran is an outlaw state. It exports terrorism; it is the major de-stabilizing force in the Middle East; and it is determined to obtain a nuclear capability.

Mr. Chairman, I was in Israel last week speaking with the highest ranking officials in the government and the military. These officials detailed the extent to which Iran funds Hezbollah in Lebanon and Hamas in the West Bank and Gaza. Iran is also the major supporter of the National Islamic Front in Sudan and also supports radical fundamentalist groups attempting to overthrow President Mubarek in Egypt. Just two months ago, General Shalikashvili, the chairman of the Joint Chiefs of Staff, revealed that Iran was deploying Hawk missile systems in the Straits of Hormuz.

Incredibly, as Iran became more and more of a threat to world peace, American oil companies became Iran's biggest oil customers, buying about \$4 billion of Iranian oil annually -- or more than 20% of Iran's total output. The oil companies can make whatever excuses they want but the shameful truth is that they put profits before patriotism and blood money before the national interest.

Mr. Chairman, this is not a partisan issue and I want to commend President Clinton for his decision to issue an Executive Order restricting American trade with Iran. This is an important first step -- but it is only a first step and it does have loopholes.

For instance, U.S. companies can continue to purchase Iranian oil through foreign subsidiaries that operate independently of the parent corporation. Also, of course, foreign companies will purchase the oil which American companies no longer buy which means that the Iranian economy will not suffer a major disruption.

Mr. Chairman, if the United States is serious about containing and restraining Iran, we must go beyond the President's executive order. We must have the will to impose real and meaningful sanctions. That is why I have introduced legislation which would not only prohibit U.S. companies from trading with Iran, it would also bar any foreign company which does business with Iran from doing business with U.S. companies--in other words, an airtight embargo.

Four years ago it took Desert Storm to dismantle the Iraqi war machine which Saddam Hussein had steadily constructed while America and the world had chosen to look the other way.

Mr. Chairman, let us learn from our experience with Iraq and take preemptive action to avoid a shooting war with Iran. Let America show true world leadership and lead an "Economic Desert Storm" against the terrorist regime in Iran. The stakes are too high for America to do less.

OPENING STATEMENT

ROBERT H. PELLETREAU
ASSISTANT SECRETARY OF STATE
FOR NEAR EASTERN AFFAIRS

Mr. Chairman, thank you for your welcome. I am pleased to join you as we discuss our efforts to make the government of Iran pay a price for its objectionable behavior. Two days ago, President Clinton boldly projected American leadership in holding Iran accountable for its unacceptable policies. On Sunday, the President announced his decision to issue an executive order banning all U.S. trade with and investment in Iran -- including the purchase of Iranian oil by American companies abroad. These new sanctions, in conjunction with our existing set of restrictions, will create a U.S. embargo against Iran.

This was not an easy decision. It was the culmination of a painstaking review of our Iran policy. This action was chosen carefully to advance those strategic U.S. interests challenged by Iran's outlaw activities. Our core concerns include: thwarting terrorism, advancing the Arab-Israeli peace process, fighting the spread of nuclear weapons, and maintaining security in the Persian Gulf. By sending a powerful political message to those who may have doubted the importance we attach to these interests, the President's recent decision will strengthen our hand as we again urge other nations to adopt our approach toward Iran. His bold action underscores America's readiness to lead by example. Only by imposing a real and heavy price can we and other countries convince the Iranian leadership that changing its threatening behavior is in Iran's own interest.

Bold American Action

The President is expected to sign the executive order very soon. The new ban will augment what was already the toughest set of existing restrictions against Iran in the world. It will prohibit trade with Iran by U.S. companies -- including overseas trade in Iranian oil -- and U.S. investment in Iran. These new sanctions were designed to build on our current prohibitions on imports into the U.S. from Iran, and on exports to Iran of sensitive goods. They will also expand the prohibition, imposed by the President in March, on U.S. financing and management of the development of Iran's petroleum resources.

The impact of the President's decision will be strong. Notably, the executive order will eliminate trade in Iranian oil by U.S. companies and their overseas branches. Last year, U.S. companies and their affiliates purchased more than 20 percent of Iranian crude oil exports. It will also eliminate U.S. exports to Iran; these sales amounted to \$326 million in 1994. It will ban the re-export of certain sensitive U.S.-origin goods. Finally, it will prevent any investment in Iran by American firms and their overseas branches.

We know that these steps will result in some costs to U.S. firms and workers. We will do what we can to limit the adverse impact. We are convinced, however, that an embargo is the most effective way our nation can achieve its goal of pressing Iran to abandon its drive to acquire devastating weapons and its support for terrorist activities.

Worsening Behavior

The President's decision to impose additional sanctions is grounded in a policy established in the early days of his Administration. With the President's support and under Secretary Christopher's stewardship, this Administration has accorded a high priority to American efforts to exert economic and political pressure on the government of Iran so as to compel a change in its threatening behavior. To maximize the pressure, we have worked along a dual track: applying unilateral restrictions and seeking multilateral cooperation in pressuring Iran. We have had some important successes, but found nonetheless that Iranian behavior in areas of concern has worsened. These disturbing trends led the Secretary to recommend to the President that he take new steps.

Let me outline the areas of concern. In particular, Iran's support of violent groups that conduct terrorist acts to undermine the peace process has increased. In defiance of the international community, the Iranian government maintains ties to rejectionist groups like the Palestinian Islamic Jihad, Hizballah, and HAMAS -- each of which has received funds, weapons, training, or logistical support from Iran.

The Iranian government has also intensified its efforts to develop weapons of mass destruction. These efforts, as well as Iran's conventional military build-up, warranted additional review. Like Congress, we have found reports of Russia's agreement to engage in nuclear cooperation with Iran particularly disturbing. Given Iran's petroleum reserves, the Tehran government's desire to obtain gas centrifuge equipment, as well as power reactors, from Russia only bolsters our conviction that Iran seeks to develop its nuclear weapons capability. Iran has also sought to acquire light water nuclear power reactors from China, and Beijing has announced its intention to go through with such a sale.

Iran's persistent pattern of support for outlaw activities led us inexorably to the following conclusion: Worsening Iranian behavior demands a response. Iran must pay a price for flouting the norms of law-abiding nations.

In taking the decision to ban all U.S. trade with and investment in Iran, President Clinton clearly signalled American determination to lead the effort among the international community in holding Iran accountable for its actions. He also intended the government of Iran to understand our seriousness of purpose. We hope our action will cause the Iranian leadership to review its policies, especially support for terrorism and the pursuit of weapons of mass destruction, and to question whether they truly serve Iran's interests.

Unmistakable Message

In making his decision, the President carefully considered the economic costs and the national security benefits of an embargo. He determined that if we are to succeed in getting other countries to make sacrifices in order to change Iran's behavior, we, too, must be willing to sacrifice. As a world leader, the onus lies on us to mobilize support. The President's bold step has reinforced our ability to secure the cooperation of all nations that share our interest in international peace and security.

Secretary Christopher has already begun to redouble our diplomatic efforts with key countries to maximize multilateral support for pressuring Iran. He is sending personal messages to our diplomatic partners, calling on them to review their economic ties with Iran. He is also asking them not to permit their firms to fill the void left by American

companies. In June, when the G-7 next meet in Halifax, the President will again urge G-7 leaders to adopt our approach. He will convey the high priority we attach to containing Iran, reiterate our mutual interest in changing objectionable Iranian behavior, and stress the need for multilateral cooperation. The President's decision will also serve as a strong basis for us to once again press the Russians and Chinese to forego nuclear cooperation with Iran.

Multilateral Cooperation

U.S. policy toward Iran has long been characterized by strong bipartisanship support. Similarly, there is general agreement among the industrialized countries on the need to bring about a change in Iran's unacceptable policies, although there have been differences on the best tactics to use to reach this goal. For example, some of the allies have argued that constructive engagement will moderate Tehran's behavior. We disagree. We believe concessionary economic policies will encourage the leadership in Tehran to think it can improve relations with the West without changing its unacceptable policies.

In recent months, some allies have pointed to U.S. economic ties with Iran -- despite the heavy unilateral limitations on this trade -- as justification for maintaining and expanding their own commercial relationships. The President's decision will eliminate that excuse, and place the U.S. in the strongest position to encourage other nations to adopt similar or parallel steps. Iran cannot stand up to coordinated pressure from all of the industrialized nations. That is exactly the goal of the President's executive order: to increase the effectiveness of our efforts to maximize pressure on Iran.

As we seek the broadest possible multilateral support, we must be careful not to jeopardize our own bilateral relationships with other industrialized nations, particularly with the G-7. In the course of our review of Iran policy, we examined the issues of extraterritoriality and a ban on financial transactions. In terms of the extraterritorial application of U.S. law, we concluded that the risk of alienating countries, whose cooperation we need to maximize the effectiveness of our policy toward Iran, outweighs any potential benefit. Our policy would not be served by launching a series of drawn-out legal battles with our closest friends. We want to isolate the Iranians -- not become isolated ourselves.

We also determined that a prohibition on all financial transactions would undermine our role in international banking. Such a ban would interfere with Iranian payments to Americans pursuant to awards rendered by the Iran-U.S. Claims Tribunal in the Hague. It could prevent us from meeting our obligations under the Algiers Accords (which ended the 1979-81 hostage crisis), and other international agreements. By contrast, our ban on investment will prevent financial transactions that could help stabilize Iran's economy without running these risks.

Conclusion

Mr. Chairman, the Administration believes it is essential to sustain the close collaboration the executive branch has shared with Congress on the issue of Iran policy. We welcome opportunities, such as today's hearing, to consult with you on this important matter. We believe the President's decision to impose additional sanctions on U.S. trade and investment with Iran will dramatically reinforce American leadership in urging our diplomatic partners to join us in pressuring Iran to change its objectionable behavior. We believe our policy deserves the support of our allies, and we hope they will respond to our lead. We hope, too, that the President's bold action will command the backing of Congress.

ECONOMIC SANCTIONS AGAINST IRAN

Statement by

Jeffrey J. Schott
Senior Fellow
Institute for International Economics

Before the

Subcommittee on International Economic Policy and Trade
Committee on International Relations
US House of Representatives

May 2, 1995

I welcome the opportunity to comment on the proposed expansion of US economic sanctions against Iran contained in H.R. 1033. My comments apply as well to the expanded sanctions included in the executive order announced on April 30 by President Clinton.

This statement draws heavily on the comprehensive analysis of 116 cases of the use of economic sanctions in the twentieth century contained in the two-volume study, Economic Sanctions Reconsidered: History and Current Policy, that I coauthored with Gary Hufbauer and Kimberly Elliott.¹ It also reflects my personal experience in the US Government with the formulation of sanctions policies against the Soviet Union, Iran, and Libya in the late 1970s and early 1980s.

My comments focus exclusively on the efficacy of economic sanctions in achieving foreign policy goals, although I recognize that sanctions episodes have important and sometimes overriding

¹ Gary Clyde Hufbauer, Jeffrey J. Schott, and Kimberly Ann Elliott, Economic Sanctions Reconsidered: History and Current Policy, 2 volumes, Washington: Institute for International Economics, second edition, 1990.

domestic policy objectives. The analysis reflects the lessons my colleagues and I derived from the extensive history of the use of sanctions as to the types of circumstances in which economic sanctions are more likely to succeed.²

Economic Sanctions: General Comments

Sanctions are one of a variety of instruments of statecraft (ranging from diplomatic to military action) designed to project power and to influence the behavior of the target country. They are usually implemented in conjunction with other policy initiatives. Several aspects of their use bear mention:

1. Contrary to conventional wisdom, sanctions can contribute to the successful achievement of foreign policy goals.³ However, the success rate depends importantly on a number of factors. Sanctions have been most effective when:

- o directed toward a limited and narrowly-defined policy goal (the more ambitious the objective, the less likely that sanctions will be effective).

- o the United States held substantial economic leverage over the target country.

² The "success" of a sanctions episode is measured by the extent to which the foreign policy outcome is achieved, and the contribution of the sanctions (as opposed to other factors such as military action) to that outcome.

³ However, over the past two decades, economic sanctions have not had a good track record in contributing to the achievement of US foreign policy objectives. See Economic Sanctions Reconsidered, chapter 5.

- o US relations with the target country had been friendly in the past, since such countries are more likely to comply with US demands in deference to the overall relationship.

- o the target country faced economic problems and domestic political turmoil, and

- o the costs to US industries affected by the sanctions were not very large.

In general, sanctions should be applied forcefully to maximize the impact on the target economy and to minimize opportunities for evasion (and offsetting assistance from third countries). These common sense guidelines were "codified" in the Institute's study in a list of "nine commandments" on the use of sanctions (Annex A).

2. Sanctions cannot be applied in laser-like fashion. They are blunt instruments that can cause general economic distress but not necessarily damage to the targeted regime (as demonstrated in the cases of Panama and Haiti).

3. A policy of economic coercion may involve the use of both carrots and sticks (e.g., foreign aid and sanctions). In the past, the United States used the threat or withdrawal of foreign aid to coerce changes in the policy of target countries (e.g., South Korea and Taiwan agreed to our nuclear nonproliferation policies in the 1970s). To a large extent, the United States no longer has carrots to offer, and thus has lost the ability to influence the behavior

of foreign countries through positive actions or the threat of the withdrawal of that aid.⁴

4. Sanctions have increasingly been deployed -- whether by plan or by accident -- as a prelude to military action. In the past decade alone, US military action has complemented or superseded economic sanctions in Libya, Panama, Grenada, Haiti, and Iraq. It is important to recognize that the escalation of US sanctions may heighten expectations at home that the sanctions will succeed, and thus increase pressure to introduce other measures to complement the economic actions if the target country does not quickly comply with US demands.

Without international support, however, the prospects that US sanctions will succeed in coercing changes in Iranian policies are not very good. The lack of multilateral sanctions may thus increase the likelihood of the threat and potential use of force.

Proposed Sanctions against Iran

US sanctions against Iran are designed to achieve three specific objectives: to halt Iran's support for terrorism, to block the proliferation of nuclear weapons to Iran, and to promote adherence to "internationally recognized standards of human rights" in Iran. The expansion of US sanctions is intended to demonstrate US resolve in countering Iranian policies, and to

⁴ While the United States could threaten to withhold economic aid to Russia if that country undercuts our nuclear nonproliferation efforts vis-a-vis Iran, we have other vital interests with Russia that would weigh against such action.

encourage other countries to follow suit, so that the sanctions reduce resources available to Iran to fund terrorist adventures and military purchases, and to weaken the ruling regime so as to foster political reform.

HR 1033 amplifies the extensive sanctions already in force against Iran under various US statutes, as well as the executive orders issued by President Clinton on March 15, 1995 prohibiting US participation in Iranian oil-field investments, and expanded this week to impose a comprehensive trade, investment, and financial embargo. Many of the sanctions are already in effect pursuant to existing statutes (e.g., terrorism list sanctions) or specific provisions of recent foreign aid appropriations acts.

In brief, the draft legislation:

- o establishes a comprehensive embargo on all US trade with Iran (except for food, clothing, and medicine for humanitarian purposes), and applies the embargo on an extraterritorial basis to overseas transactions by US citizens or corporations.

- o prohibits all financial transactions involving Iran or any Iranian national (which also seems to encompass a freeze of US assets of Iranian nationals).

- o tightens export licensing controls to prevent reexportation to Iran of "any item or technology controlled under the Export Administration Act of 1979, the Arms Export Control Act, or the Atomic Energy Act of 1954."

- o requires US opposition to all assistance to Iran from international financial institutions and UN agencies.

o allows the President to remove the sanctions if he determines and certifies to the Congress that Iranian policies regarding human rights, arms proliferation, and terrorism have been substantially altered to meet US demands.

Can the US sanctions achieve their foreign policy objectives?

The objectives of the US sanctions are praiseworthy, and deserve greater international support than they are evidently receiving. The policy changes demanded of Iran are specific and relatively limited, unless the human rights objective is interpreted broadly to require a major change in the Iranian regime. In past episodes, such narrowly focused goals have been more achievable than other goals that sought more fundamental changes in the ruling regime of the target country. However, those previous successes involved target countries that were heavily dependent on the United States for economic support and military assistance.

Overall, I am skeptical that unilateral US economic sanctions will promote significant reform of Iranian policies. The sanctions have too little bite, have little support among other countries (and may well cause frictions with our G-7 allies), and are likely to be offset by a brigade of "black knights".

In brief, US sanctions against Iran observe several of the "Nine Commandments", but violate several others. On the plus

side, the sanctions are targeted against a much smaller country already suffering economically.

However, existing trade relations with Iran are minimal after 16 years of acrimonious relations since the Iranian revolution. Direct US exports -- which have averaged about \$550 million annually for the past three years -- account for less than 4 percent of total Iranian imports. The comprehensive US trade embargo would cut off almost all of those exports. Such action would cost US companies a substantial amount of sales to Iran, but would cost Iran very little since most of those products can be purchased from other foreign suppliers.

Compared to the overall size of the US economy, the cost to US companies from the Iran sanctions would be minimal. That conclusion holds even if one extends the embargo to all US shipments and assumes that the extraterritorial application of US sanctions forces US oil companies to forego trading profits on 750,000 bbl./day of Iranian crude. Nonetheless, forgoing hundreds of millions of dollars of US exports seems to be a high price for sanctions which many consider only to be of symbolic value.

In addition, three issues deserve more detailed comment: the cost of the sanctions to Iran, problems created by the extraterritorial application of the sanctions, and the problem of offsetting assistance from "Black Knights".

Revenue Effect. As noted above, the sanctions are designed to limit the resources available to Iran to finance its terrorist adventures and weapons acquisitions. A similar rationale was used for the US embargo of Libyan oil in the early 1980s.

I am highly skeptical that unilateral sanctions can significantly reduce current and potential Iranian oil revenues. The reason for that conclusion is simple: fluctuations in world oil prices have a much more dramatic effect!⁵ In just the past few months, oil prices have increased about \$2/bbl due to strong global demand and uneasiness about developments in the Gulf, generating an additional \$5 million a day (or about \$1.75 billion per year) for Iran. Extraterritorial application of US sanctions to block purchases by foreign subsidiaries of US oil companies would not decrease Iranian exports (since the distribution of those shipments could be easily handled by non-US companies), and would reduce Iranian revenues by only a small fraction of the amount generated by higher world oil prices.

Extraterritorial Application of US Sanctions. There are several precedents for the extraterritorial application of US sanctions, but none of them are good ones. Perhaps the worst example occurred in the early 1980s, when the United States attempted to block foreign subsidiaries of US corporations from supplying equipment for the construction of a gas pipeline from

⁵ In the Libyan case, oil revenues were reduced, not because of the US embargo, but because of the sharp drop in world oil prices in the face of global recession.

the Soviet Union to Europe.⁶ The US action provoked a furor in Europe and prompted several governments to institute anti-boycott legislation to bar companies from complying with the sanctions.⁷ The extraterritorial application of the US sanctions provoked legal disputes and diplomatic rows with our European trading partners, and ultimately did little except to distract attention away from the avowed target.

Broad application of the US sanctions to foreign subsidiaries of US companies could elicit the same response in Europe, and perversely undercut efforts to build a multilateral consensus in favor of expanding sanctions against Iran. If such action is taken, it would be preferable to limit extraterritorial application to the distribution of crude oil in order to narrow the scope of potential conflict with our allies.

A similar argument applies to legislative proposals to enact a secondary embargo, blocking access to the US market for firms that do business with Iran. Such an embargo would likely violate US international trade obligations when imposed against trade from member countries of the World Trade Organization, would exacerbate tensions between the United States and our allies, and thus greatly diminish prospects for multilateral action against Iran.

⁶ The case is fully documented in the IIE study.

⁷ In many respects, these laws are similar to the US anti-boycott provisions designed to counter the Arab boycott of Israel.

Offsetting International Assistance for Iran. The United States faces two problems in seeking international support for its sanctions policy against Iran. First, and to put it bluntly, US allies do not put as high a priority on punishing Iran for its inflammatory policies as we do, nor do they have the same willingness to sacrifice short-run commercial profits to demonstrate outrage against Iranian practices. The G-7 countries do control the export to Iran of dual-use items, but continue to trade extensively with Iran and to extend substantial amounts of trade and development finance.

It is hard to explain the G-7 response to US overtures. Europe and Japan would seem to be more vulnerable to renewed conflict in the region and the potential cut-off of oil flows from all sources that ship through the Persian Gulf. Moreover, Europe has been the host to a variety of terrorist acts planned and/or financed by Iran.

In my view, European reluctance to join in expanded sanctions probably reflects both their belief that sanctions alone won't influence Iran's leaders, and their unwillingness to risk an escalation of the sanctions in the form of increased political and military pressure (in light of their vulnerabilities, cited above). I dismiss as extremely naive the claim that European opposition to the less-than-total US embargo reflects doubts about our commitment to counter Iranian transgressions.

A second and related problem involves other countries that are willing to supply sanctioned goods to Iran. Iran has a brigade of "Black Knights," willing and able to supply it with arms and material and nuclear technologies. Even if these supplies are not up to the world class standards of products and technologies controlled by the G-7 powers, they are dangerous enough to cause serious trouble. Black Knights like Russia and China are even more driven by the profit-motive than the industrial economies of Europe and Japan.

To date, diplomatic pledges from these countries have had limited value. Some countries, like China, ignore our entreaties. Others like Russia, have not yet implemented their vague promise to control technology transfer (witness the \$1 billion contract to supply 4 light water reactors to Iran, their offer of technical assistance and training in nuclear technologies, and recent Russian sales of jet fighters and missiles). President Clinton should demand that such sales to Iran be nullified when he meets with President Yeltsin next week.

Annex A. The Nine Commandments of Sanctions Policy

I. "Don't Bite Off More Than You Can Chew."

Policymakers often have inflated expectations of what sanctions can accomplish. Sanctions are seldom effective in impairing the military potential of an important power, or in bringing about major changes in the policies of the target country.

II. "More Is Not Necessarily Merrier."

In general, the greater the number of countries needed to implement sanctions, the less likely they will be effective. A country looks to its allies for help when its goals are ambitious; in cases involving more modest goals, such cooperation is not needed. Moreover, when a sender country has found it necessary to seek cooperation from other countries, it was probably pursuing a sufficiently difficult objective that the prospects for ultimate success were not bright. On the other hand, active noncooperation can sabotage a sanctions effort. Offsetting assistance given to the target country by a third country erodes the chances of sender-country success.

III. "The Weakest Go to the Wall."

Countries in distress or experiencing significant economic and political problems are far more likely to succumb to coercion by the sender country. Most target countries have much smaller economies than the countries imposing sanctions. However, the relative size of the target economy is less important than other factors that come into play, such as the extent of trade linkage, the economic impact of the sanctions, and the warmth of relations between sender and target prior to the imposition of sanctions.

IV. "Attack Your Allies, Not Your Adversaries."

Economic sanctions seem most effective when aimed against erstwhile friends and close trading partners. In contrast, sanctions directed against target countries that have long been adversaries of the sender country, or against targets that have little trade with the sender country, are generally less successful. The higher compliance with sanctions by allies and trading partners reflects their willingness to bend on specific issues in deference to an overall relationship with the sender country.

V. "When 'Tis Done, Then 'Twere Well It Were Done Quickly."

Sanctions imposed slowly or incrementally may simply help the target government withstand the foreign pressure. A heavy, slow hand invites both evasion and the mobilization of domestic opinion in the target country. Time affords the target the opportunity to adjust: to find alternative suppliers, to build new alliances, and to mobilize domestic

opinion in support of its policies. As such, a strategy of "turning the screw" on a target country, slowly applying more and more economic pressure over time, is generally counterproductive.

VI. "In for a Penny, In for a Pound."

Cases that inflict heavy costs on the target country are more likely to be successful. If sanctions can be imposed in a comprehensive manner, the chances of success improve. However, there is a "black knight corollary" to this conclusion: sanctions that attract offsetting support from a major power may cost the target country little on a net basis and are less likely to succeed.

VII. "If You Need to Ask the Price, You Can't Afford the Yacht."

The more it costs a sender country to impose sanctions, the less likely it is that the sanctions will succeed. A country should shy away from deploying sanctions when the economic costs to itself are high. Countries that shoot themselves in the foot may not mortally wound their intended targets.

VIII. "Choose the Right Tool for the Job."

Economic sanctions are often deployed in conjunction with other measures, such as covert action, quasi-military measures, or regular military operations. There is little correlation, however, between the use of companion policies and increased effectiveness. Rather than buttressing a sanctions campaign, companion measures are frequently used when sanctions are perceived to be either wholly inadequate or simply too slow.

IX. "Look Before You Leap."

Sender governments should think through their means and objectives before taking a final decision to deploy sanctions: they should be confident that their goals are within their reach, that they can impose sufficient economic pain to command the attention of the target country, that their efforts will not prompt offsetting policies by other powers, and that the sanctions chosen will not impose insupportable costs on their domestic constituents and foreign allies. These conditions will arise only infrequently.

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I am Arthur T. Downey, Vice President of Baker Hughes Incorporated, a *Fortune* 200 Company headquartered in Texas, but I appear today on behalf of the National Foreign Trade Council. The National Foreign Trade Council is an association of more than 500 US companies engaged in international trade and investment. We are grateful for this opportunity to be heard and for the balance of views you have assembled at this hearing.

* * *

In this testimony, I will try to explain why we believe a broad based unilateral embargo will be ineffective (pages 3-5) and why extraterritoriality is troublesome (pages 5-6). The bulk of my focus will be to point out what we believe are the costs of this embargo (pages 6-12), and what we expect to happen if the broad embargo is enacted (pages 12-13). We also offer specific alternative approaches that we believe might be more effective at less cost (pages 13-15). Finally, we also take note of what we believe to

be an imbalance in the Congressional/Executive balance with respect to foreign trade authority (pages 15-16).

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We are in union with what we understand to be the basic goals of those advocating sanctions against Iran: to turn Iran from its State supported terrorism, and to prevent it from acquiring weapons of mass destruction. These goals are very important to the US national interest, and, indeed, they are in the best interests of the world community. The US business community is not the enemy.

The issue on the table is not the goals, but the method--how can the US most effectively achieve these goals? That answer entails weighing costs and benefits, and looking realistically at the world around us.

One method, advocated by Representative King, is to impose a broad, unilateral, extraterritorial embargo on transactions with Iran and with Iranian nationals. We believe that approach is misguided, because it will be ineffective in achieving the goals, and it will also be costly to US international competitiveness, and ultimately to US jobs.

Representative King also proposes a secondary boycott against foreign companies. Turning attention from hurting American companies to pressuring foreign competitors has a certain emotional appeal. However, responsible members of the business community cannot support such a secondary boycott. As we know from other contexts, such as the Israeli-Arab conflict, secondary boycotts are fundamentally harmful to the global trading and investment system.

It is worth remembering that both these proposed sanctions are vastly more severe than the measures imposed by the US against the Soviet Union at the deepest point in the Cold War.

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I. Why is such an embargo ineffective? By virtue of the unilateral nature of the proposed broad embargo, the rest of the world--allies and competitors--can, and will, continue to trade with Iran, and to supply it with virtually any product or service it currently obtains from the US. Iran's oil will continue to be bought, by non-US oil companies. The economic/commercial impact on Iran of this embargo will be fleeting at best.

Over a great many years, the US has tried unilateral embargoes, and the evidence is overwhelming that they simply do not work. Indeed, most studies show that the costs are greater for the US than for the targeted country. (Remember the grain and pipeline embargoes against the Soviet Union.) The GAO reported last November the results of its study which concluded that a unilateral US embargo on Nigerian oil would have "almost no impact". This is in sharp contrast to a multilateral embargo, which the GAO believed could have a "significant economic effect." The last GAO study of general economic sanctions was prepared in 1992, and is worth your serious attention.

The single clear exception to the general proposition that unilateral sanctions are ineffective may be in the situation where the US enjoys a monopoly on a certain product or technology. Restricting those from the target country could, depending upon the specific situation, be effective by having an impact on the target. But, such unilateral restrictions would have to be applied with flexibility and on a case-by-case basis. In the case of Iran, virtually all of their imports from the US are readily available from non-US sources.

The sanctions against Libya might be an interesting case to study. It

seems generally agreed that the massive US unilateral economic sanctions since the mid-1980's have been ineffective in that they have had little impact on Libya. However, it seems also generally agreed that the more recent UN-mandated, multilateral sanctions--those springing from the PamAm tragedy--have indeed caused some pain in Libya, and may well be effective in causing some change in Libya's behavior. And the bottom line is: multilateral sanctions tend to work; unilateral sanctions almost always do not.

If there is any doubt on the part of the Committee with respect to the impotence of a unilateral embargo, we would urge that the Committee seek an investigation by the GAO or any other objective and respected body. Needless to say, that effort should be accomplished before new unilateral sanctions are legislated, not after.

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II. Why is extraterritoriality troublesome? The proposed embargo tries to regulate conduct of companies incorporated under the laws of other countries, on the grounds that those companies are owned or controlled by US companies. The fact is that the rest of the world--including our allies and

friends--believes that international law does not allow the US the right to reach that far. Our closest friends, such as the Canadians and British, have enacted laws that block any such US attempt. US foreign subsidiaries are put in the position of having to violate US law or local law.

Such an attempted thrust by the US would be met with strong resistance by otherwise friendly and supportive governments. **Getting into a fight with our foreign friends over sovereignty is not what we need, and will be counterproductive to the larger US interests in persuading them to join with us in pressuring Iran to change its behavior.** *The New York Times* of March 11 noted correctly that such foreign resentment could impede cooperation in the vital issue of preventing Iran from developing nuclear weapons. Therefore, the extraterritorial aspects of the bill not only will be ineffective, but counterproductive. In testimony in March, regarding the companion bills in the Senate, Under Secretary Tarnoff said that:"...the active cooperation of our Allies is essential. The need for multilateral action to support this endeavor cannot be overstated." We agree.

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III. What are the costs? It may be that any cost is too high in relation to a sanction that produces zero beneficial effect. But, the costs are high even in absolute terms with respect to American competitiveness in the world market. The Council on Competitiveness recently analyzed eight case studies of the impact of unilateral controls on selected products. This study found that \$6 billion in US exports and 120,000 jobs were put at risk.

A. The loss of direct US exports to Iran is not significant to the overall US economy, although total US-Iran trade last year was over \$300 million dollars (not including services) -- and those exports supported a lot of good American jobs. Those exports included frozen chickens, auto parts, soybean oil and oil field equipment.

B. Within the context of bilateral US-Iran trade, you should also be aware that American companies are owed hundreds of millions of dollars by Iran. This debt is normal, routine, international trade debt for products and services already provided--not broad, untied financing. If the US imposes the proposed broad sanctions against Iran, you can be absolutely certain that Iran will stop paying down that debt the very next day. Who suffers? Not Iran, since it will have more hard currency to spend that otherwise would have gone to reducing its trade debt to Americans. The loser will be the

American companies who will not get paid. Many of these are small companies, for whom a couple of million dollars in unpaid debt could force them into bankruptcy. The impact on US employment is obvious.

If this situation unfolds, the result will be ironic: **the action of the US Government will result in Iran receiving free American products, at the expense of American companies.**

C. **Beyond Iran, this proposed embargo reaches to regional activities, for example to bar US participation in many projects involving some of the countries of the former Soviet Union.** These are countries looking to the West, and to the US particularly, to help them achieve and maintain real independence. Precluding US involvement in regional development is counterproductive to the very policy the Bill seeks to espouse. Indeed, any foreign competitor could defeat an American company's participation in a multilateral project outside Iran simply by giving a single share in the project to an Iranian entity. Thus, the broad over-reach of the proposed transactions controls would make American companies hostage to Iran's activity and the cleverness of foreign competitors.

D. Most importantly, a total unilateral extraterritorial embargo, as proposed by Mr. King's bill, will make it absolutely certain in the minds of America's foreign customers that American companies are simply unreliable suppliers. Every day, foreign companies who are potential buyers of US products or services "design in" non-US equipment. For example, Airbus moved away from its sole reliance on US engines in large part to allow it to compete in markets closed unilaterally by the US. Not because US engines were not competitive, but because the US Government had made the US engine companies unreliable suppliers. Once foreign buyers have made their "switch" to non-US sources, it becomes highly likely that they won't switch back once the sanctions have been terminated. Airbus became the sole supplier to a segment of the world aircraft market denied to US suppliers. Thus, US sanctions policy helped to strengthen a major US foreign competitor.

E. There is also a significant beneficial impact on our foreign competitors, and it is dangerous. Put yourself in the shoes of a small foreign competitor--for example, a hypothetical French manufacturer of oil field safety equipment. The US has been the dominant supplier worldwide, and it has not been easy for that French company to break into the competitive market in any big way. However, in this hypothetical situation, the US

companies would be frozen out of the Iran market because of the unilateral US embargo. The French company would then be able to supply the Iran market--and, most importantly, it will be able to **substantially increase its profit margin**, because the US competition has just been removed.

There is another step. That hypothetical French company would then be in a position to draw on its "excess profits" to subsidize its pricing in other markets where American companies are still allowed to compete. The result: the French competition is given the financial strength to take away market share from American companies in other markets non-Iranian. Once again, the irony is overwhelming--the US Government would be assisting foreigners to compete better against American companies in the global marketplace. This is, of course, not just theory. Talk to the Caterpillar Company about their experience competing against Komatsu of Japan in non-Soviet markets when, fifteen years ago, the US Government imposed the unilateral embargo against the USSR.

F. The US Government expects much of US employers: create jobs, fund research and charities, pay taxes, provide health care for employees, etc. America also expects, demands, and needs US companies to be competitive on the international scene, especially to expand exports in

order to reduce the massive and unhealthy balance of payments deficit. (Ironically, the US Government often looks to US business to establish commercial ties in foreign countries to strengthen US diplomatic relationships.)

The Commerce Department quite properly has identified the Big Emerging Markets (BEM) which it believes will be the source of the growth in US exports. Most of these markets are risky for US companies, because of political instability, risk of expropriation, unfair trading practices (including corruption), or other foreign sourced problems. But, American companies have to be risk-takers, though they must not take unreasonable risks with their shareholders' money. How ironic that one of the biggest risks--one that cannot be insured against--is that US Government might unilaterally impose economic sanctions against one or most of those BEM's because of non-proliferation concerns, or human rights concerns, or any number of other legitimate concerns. Many US companies will decide not to take the risk.

We are competitive. But, proposals such as Mr. King's make that task unnecessarily difficult. **If this Bill became law, the only people cheering will be our foreign competitors.** As a former Secretary of State observed,

"light switch diplomacy" serves neither diplomacy nor the economic health of the US.

It is important that you recognize why no American company complains about the embargo against Iraq despite the costs. In the case of Iraq, the embargo has been effective, but it is not extraterritorial, and the costs are shared multilaterally --by all companies, US and non-US. All competitors bear the same burden, and the US companies are not singled out and branded as unreliable.

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IV. What will happen if these bills are enacted? The consequences of the enactment are quite predictable:

(i) Iran will have evidence to show to those nations and groups that it seeks to cultivate that the US has launched a new phase in its economic warfare with Iran, that the US is alone in its fight with Iran;

(ii) at the commercial/economic level, Iran will quickly shift its few US relationships to other countries, suffering no ill effects from the embargo;

(iii) companies all over Europe and Japan will surely celebrate the forced retreat of American competition;

(iv) Iran will applaud as governments closest to the US act to block the US attempted control over their companies; and

(v) in the longer term, foreign buyers will design out US products and services, because US companies are unreliable, and American companies will be less willing to take risks in the Big Emerging Markets.

Thus, this broad, unilateral, extraterritorial embargo will be no more effective in getting Iran to alter its actions than if this Committee's Members were to go on a hunger strike. Worse, it would carry broad, long-term costs to American competitiveness. It will not result in isolating Iran from the rest of the world, but rather, the US will isolate itself for no real gain. No US interest is served by acting, as another former Secretary of State has said, with a "sullen unilateralism that bashes our allies."

V. What should the US do: Is there an alternative that might be effective at less cost? There is no simple solution, no magic wand. The right course is the hard course: the US Government must re-double its

leadership efforts to obtain broad multilateral agreement on the dangerous aspects of Iran's activity, and then to insist that America's friends and allies join with us and share the burden in a multilateral effort. That is the exercise of real leadership. Only in that way is there any chance of effectively altering Iran's behavior.

If we clearly define our goals to focus on Iran's State supported terrorism, and Iran's efforts to acquire weapons of mass destruction, there are steps that could be taken, even outside the area of economic sanctions. If the threat is so deadly serious, should not covert action be employed? If Iran is a democracy (however primitive and corrupt)--unlike the dictatorship in Iraq--would not massive doses of information and engagement ultimately force a change in behavior? Surely, the regime in Tehran would be more threatened by broadcasts of CNN (or even MTV) than not being able to buy American frozen chickens.

Economic sanctions can also play a role. **The NFTC offered a specific and detailed proposal to the Administration.** This proposal would target goods, technology and services that enhance the ability of Iran to support acts of terrorism, and would focus on specific entities engaged in weapons proliferation. The proposal also would prohibit US persons from direct

investment in Iranian infrastructure projects. To ensure multilateral effectiveness, the proposal urges the US to obtain the agreement of other nations to impose equivalent sanctions for their citizens. It would be very difficult for responsible members of the international community to refuse to join in such a very targeted effort.

The result would be effective action against the most dangerous part of Iranian behavior. Importantly, the US would be leading the world, not conflicting with it--and that might well lead to multilateral steps for broader sanctions as well.

Another alternative would be to adopt the approach taken in Mr. King's embargo Bill, without the extraterritorial provisions -- but make the law effective upon the certification by the President that the other relevant countries agreed to join with us. At that point, the sanctions become multilateral, and therefore effective, without loss of America's competitive position. The initial adoption would "signal" our Allies that the US was serious and wanted effective action; that type of leadership likely would work.

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VI. We would be remiss if we failed to acknowledge the fact that the President has said he will issue an Executive Order which adopts much of Mr. King's Bill. This anticipated Presidential Order action casts a large shadow over this debate. Such action would be based on a declaration by the President of a "national emergency" and a finding that actions of Iran constituted "an unusual and extraordinary threat to the national security, foreign policy, and economy of the United States", under the International Emergency Economic Powers Act.

We believe that Presidents--of both political parties--have taken excessive liberty in finding these "unusual" and "extraordinary" "emergencies." Regrettably, there has been little Congressional reaction. Therefore, we urge the Committee to consider reviewing this broad grant of authority from the Congress to the Executive. Perhaps the time has come to return some of that foreign trade power to the Congress, where the Constitution places it.

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Our final plea is for reasoned judgment. We urge you not to proceed in emotional haste just to satisfy the natural desires to "do something" or to

"feel good." What is the urgency? Why the rush? Why not instruct the GAO to investigate the likely effectiveness of alternative approaches? Why not instruct the Congressional Budget Office to evaluate the costs of alternative approaches? The reasonable decision-tree considerations laid out in Section 6 of the late Export Administration Act would be a good place to start those inquiries.

We believe the most important first step in the consideration of economic sanctions is to have a clear and honest statement of the goals. Too often, domestic politics, or emotional frustration, has led the US automatically to default to economic sanctions, because they seem at first blush to be "cost-free". Rational decision-making should ensure that the Congress (or the President) be able to state clearly exactly what is the goal, a goal that is realistic and measurable? Measurability is very significant, because otherwise you will never know whether the approach has been successful or has failed (and thus should be withdrawn).

If the broad unilateral embargo is enacted, the consequences will be the equivalent of a billion dollar tax over time levied only on American companies, but where the proceeds flow not to the US Treasury, but to America's competitors overseas. We can assure you of that. It is up to Members of Congress to assure themselves, with an equal certainty, that this cost will be more than offset by the benefits you hope to achieve.

Testimony of

Geoffrey Kemp
Carnegie Endowment for International Peace

US Policy Toward Iran; Do New Sanctions Make Sense?

Introduction

Iran poses several distinct threats to American interests in the Middle East. We need to distinguish short-term from long-term threats and direct from indirect threats. There is increasing consensus between the United States, several of its European allies, Japan, Israel, and many Arab countries that Iran behaves in ways that are inimicable to Western interests. Of particular concern is Iran's putative nuclear and missile program, its conventional military modernization program that could challenge U.S. maritime supremacy in the Gulf and its adjacent waters, and its avid opposition to the Arab-Israeli Peace Process, including support for radicals and terrorists intent upon destroying the Israeli/Palestinian accords. *Of these concerns, Iran's nuclear ambitions are by far the most serious and warrant priority action to be taken jointly with our key allies. The wisdom of new sanctions should be measured against this primary yardstick -- will they reduce the probability that Iran will obtain nuclear weapons in the next 10 years or so?*

The current debate in Washington is not about the nature of Iranian behavior -- there is virtual consensus that it is unacceptable. It is about the

costs and benefits to United States interests of imposing increased sanctions against Iran including greater restrictions on trade and penalties against foreign governments and companies that sell Iran strategic items that can assist in its weapons of mass destruction programs and its overall economic well being.

US Efforts to Contain Iran

The Administration has enunciated a policy of dual containment for confronting both Iraq and Iran. The policy includes military strategies designed to deter, and if necessary defeat, any Iraqi or Iranian military aggression in the Gulf. Since the Gulf War, U.S. military cooperation with Arab allies in the GCC has grown and the forces we have earmarked for possible intervention are well equipped and prepared for most short-term contingencies. The Administration has also orchestrated a political and economic campaign to continue UN sanctions against Iraq and to try to isolate and weaken Iran -- which is not subject to UN sanctions -- and put pressure on the Islamic regime to change its ways. This latter policy has only been partially successful and we have been roundly criticized for continuing a flourishing economic relationship with Iran while calling on allies to reduce their own commerce with the regime. This explains why President Clinton announced on April 30th that he would sign an Executive Order essentially ending all U.S. trade with Iran. A related reason for

this action is the Administration's hope that it will pre-empt much more draconian measures proposed by the Congress, especially a draft bill submitted by Senator D'Amato.

Both Administration and Congressional efforts to impose more sanctions against Iran must be examined in the context of costs and benefits to American and Iranian interests, as well as the likely reaction of Iran's key economic partners such as Germany and Japan and its suppliers of military technology, especially Russia, China and North Korea. It is essential that the long-term implications of proposed sanctions legislation be widely debated. Given the current universal antagonism towards Iran in the United States it will be easy to pass laws that seem tough at the time but eventually could rebound to our disfavor.

- Will increased sanctions weaken the Islamic regime to the point when its leaders will adopt more moderate policies or will they make its leaders more defiant and dangerous in the short run?
- Will our allies take seriously new Congressional legislation or will they ignore our homilies and continue business as usual with Teheran?
- How will U.S. economic interests be affected by the proposed legislation?

In this testimony I will focus on the first two questions which are more political in nature.

Some would use the example of Iraq to suggest that desperate regimes do desperate things. They argue that it was economic desperation that led Saddam Hussein to use his considerable military assets against Kuwait in August 1990. Had he used his military assets in a more Machiavellian manner he could have achieved his goals without embarking on a war with the rest of the world. Iran, it could be argued, may find itself in a similar predicament if sanctions are tightened and it's economy continues to deteriorate. A desperate regime, dominated by radicals, could use its limited military assets not to invade a neighbor, such as Kuwait -- they simply do not have the assets to do that -- but to change the nature of confrontation in the Gulf. Some have postulated that Iranian submarines could lay mines in shipping lanes or use its shore-based missiles to attack tankers and try to block the Straits of Hormuz. The purpose would not be to achieve any maritime victory over the United States but rather to sow panic through the oil markets and to put the Arab Gulf on notice that Iran will not sit back and allow its revolution to be squashed.

In such circumstances United States military assets are adequate to ultimately defeat any Iranian military action although whether a limited engagement would be in American interest is another matter. On the other hand, escalation to a full-scale war with Iran would pose an enormous set of problems for the United States both militarily and politically. These types of

threats could evolve in the coming months or years if those who believe the Iranians, when cornered, will strike out, are correct.

An alternative view would be that Iran is in dire economic straits and now has to be careful about further isolating itself from the rest of the world - as it would by interfering with oil traffic. Rather, it will have to reach out and make compromises, not necessarily with the West, but with other neighbors, to avoid a domestic implosion which could be triggered due to economic deprivation and social unrest. They point to Iran's relations with Russia, the Caucasus, and Central and South Asia to show the pragmatic and nationalist nature of its foreign policy.

The most persuasive political arguments for tighter restrictions on U.S. exports to Iran and the purchase of Iranian oil by U.S. companies are that unless the U.S. is prepared to make economic sacrifices to implement its policy of containment, it has no moral authority to plead with others to deny themselves access to the Iranian market. It has been difficult to convince allies of our seriousness so long as we remain one of Iran's key trading partners and our oil companies buy billions of dollars of Iranian oil. Stopping U.S. oil companies from doing business with Iran may not initially change Iranian behavior but it certainly makes it easier for the U.S. government to demonstrate

its resolve. *However this approach alone will be insufficient to persuade our allies and friends to tighten economic pressures on Iran.*

The Importance of the Nuclear Issue

The most compelling case to be made for tougher sanctions against Iran concerns its activities with respect to nuclear and missile development. There are two routes Iran can follow to get the bomb. First -- by openly proceeding with its civil nuclear program with the cooperation of Russia and China, Iran will develop a nuclear infrastructure and a trained cadre of engineers and scientists who will be familiar enough with the process to make it possible for Iran to move toward a nuclear weapons program were it to ever formally withdraw from the nonproliferation treaty, as it is legally permitted to do. The second route, the covert route, would be to cheat on its NPT commitments and go ahead with efforts to jump-start a nuclear weapons program using technology and support procured from the black market. This route would undoubtedly shorten the time frame needed for Iran to get the bomb, but it runs the risks of being discovered and triggering economic sanctions not just from the United States, Europe and Japan, but from the United Nations as well.

The preferred American policy must be to orchestrate and sustain

multilateral containment of Iran. The more conclusive the evidence that Iran is undertaking a serious nuclear weapons program in violation of its NPT commitments, the easier it will be to persuade the allies, especially the West Europeans and Japan, that business as usual with Teheran has no impact on moderating Iranian behavior in this most critical arena. There is evidence that American overtures are already beginning to have some impact on Britain, France and Japan. Additional homilies concerning Iran's appalling human rights record, its support for terrorism and its opposition to the Arab-Israel Peace Process, while important, are likely to be less persuasive. *Japan appears to be having second thoughts about its huge hydro-electric program in Iran. Convincing Germany to change its current policy towards trade with Iran will be more difficult and remains one of the highest priorities.*

To convince Russia to back down from its avowed intention of selling Iran nuclear reactors and possibly centrifuge technology requires both sticks and carrots. The new legislation proposed by Senators McCain and Lieberman and Congressman Lantos focuses on penalties for Russia if it continues with the sales. The McCain and Lieberman bill would strengthen the existing Iran-Iraq Arms Non-Proliferation Act of 1992. The proposed Lantos bill would put Russia on notice that if it proceeds with its nuclear sales programs to Iran it will forfeit further American economic assistance (aside from that earmarked under Nunn-

Lugar to dismantle and control nuclear weapons in the Former Soviet Union).

But Russia will not back down on this sale unless some carrots are offered, preferably as part of an overall review of US-Russian policy on technology transfers worldwide. Russia feels that the United States has purposely set out to deny it access to lucrative markets for its arms and technology in India, Southeast Asia, East Europe and the Arab Gulf; that it refused to offer Russia any part of the multi-billion nuclear deal negotiated with North Korea; that it wishes to pursue an arms embargo on Iraq indefinitely and that Russian arms sales to Iran should be stopped while extremely lucrative U.S. sales to the Arab Gulf proceed, even as the U.S. calls for the extension of NATO to Russia's doorstep. *Unless some tacit market sharing agreement is negotiated, the bureaucratic and economic pressures on Russia to conclude legal sales of nuclear technology and conventional arms to Iran will continue.*

As for the more sweeping legislation proposed by Senator D'Amato, it runs the risks of being too divisive with our allies and too impractical at this time. Clearly some of the proposals in the comprehensive Iran Sanctions Act of 1994 (s-277) can be implemented without creating real problems with our allies (e.g. end our own direct trade with Iran and tighten restrictions on support to Iran from multilateral financial institutions we support). However it is not

going to be easy to implement these laws, let alone the additional laws proposed to sanction foreign companies that trade with Iran.

The most troublesome effect of the more sweeping legislative proposals to contain Iran may be to anger many of our friends and allies and to dilute our more focused efforts to deal with the priority nuclear problem. However, if over the coming months the Administration can produce incontrovertible evidence of Iranian malfeasance on the nuclear issues, *the threat of the D'Amato legislation might be a useful tool for the Administration to have up its sleeve.* In the meantime, the best policy will be to allow time to see if the new Executive Order has a positive impact on allied behavior. If it does not, then the tougher proposals will deserve a second hearing.



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In the 1970s he worked in the Defense Department in the Policy Planning and Program Analysis and Evaluation Offices and made major contributions to studies on U.S. security policy and options for South West Asia. While working for the Committee on Foreign Relations, U.S. Senate in 1976 he prepared a widely publicized report on U.S. Military Sales to Iran.

From 1970 to 1980, he was on the faculty of the Fletcher School of Law and Diplomacy, Tufts University. He is the author of The Control of the Middle East Arms Race, co-editor of Arms Control and Weapons Proliferation in the Middle East and South Asia, co-author of India and America After the Cold War, and most recently, author of Forever Enemies?: American Policy and the Islamic Republic of Iran published in April 1994.

U.S. Goals Towards Iran -- Will Comprehensive Sanctions Help?¹

Statement to the House International Relations
 Subcommittee on International International Economic Policy and Trade
 by Patrick Clawson,² May 2, 1995

Before answering the question of whether the comprehensive sanctions on Iran announced by President Clinton will advance U.S. policy interests, it is necessary to determine what are U.S. policy goals towards the Islamic Republic of Iran. Indeed, much of the debate about Iran sanctions has been in fact a debate about what is an appropriate goal for U.S. Iran policy.

Policy Options towards Iran

The most basic difference among policy options towards Iran is over what is the desired end state. There are four possibilities: accepting Iran as it now is, seeking a modification in Iranian behavior, containing Iran until such time as the Islamic Republic collapses, and actively promoting the overthrow of the Islamic Republic.

The first option is not acceptable to the U.S. Let us examine in turn the other options, asking to what extent each is the actual basis for existing U.S. policy and what are the advantages and disadvantages of each.

Carrots and Sticks

Despite a widespread misperception, U.S. policy accepts the Islamic Republic in Iran and only wants to change its behavior. In Martin Indyk's speech on the "dual containment" policy (to The Washington Institute for Near East Policy, May 21, 1993), he was careful to hold the

¹ The views expressed here are those of Dr. Clawson alone. They do not necessarily represent the position of the National Defense University, the Department of Defense, or the U.S. Government.

² Dr. Clawson is a senior fellow at the Institute for National Strategic Studies of the National Defense University. His most recent books are *Iran's Strategic Intentions and Capabilities* (NDU Press, 1994); *How Has Saddam Hussein Survived? Economic Sanctions 1990-93* (NDU Press, 1993); and *Iran's Challenge to the West: How, When, and Why* (The Washington Institute for Near East Policy, 1993). From 1981 through 1992, he was a research economist for four years each at the International Monetary Fund, the World Bank, and the Foreign Policy Research Institute, where he was also the editor of *Orbis*, a quarterly review of foreign affairs. He has been a visiting fellow on several occasions at The Washington Institute for Near East Policy. He is currently senior editor of *Middle East Quarterly*.

hope for normal relations with Islamic Iran:

I should emphasize that the Clinton administration is not opposed to Islamic government in Iran. Indeed, we have excellent relations with a number of Islamic governments. Rather, we are firmly opposed to these specific aspects of the Iranian regime's behavior, as well as its abuse of the human rights of the Iranian people. We do not seek a confrontation, but we will not normalize relations with Iran until and unless Iran's policies change, across the board.

That continues to be U.S. policy, as enunciated frequently by Assistant Secretary Pelletreau.

The implicit thesis behind this policy seems to be: limit excesses while awaiting the triumph of the moderates. In many ways, the U.S. policy is quite close to the European and Japanese view. All accept that they could live with the Islamic Republic if only it were run by moderates. The aim of the Western powers seems to be modification of Iranian behavior through a nuanced policy of rewarding positive steps and penalizing negative actions. Most European governments talk about their Iran policy as reinforcing those tendencies of which they approve, while using the leverage this gives them to seek change on those matters which they dislike. That is formulation that stresses the carrot part of the carrot and stick policy; indeed, carrots have been more in evidence from Europe than have sticks.

The U.S. government's policy seems to be largely the same carrot and stick policy, but with more liberal use of the stick and a more sparing offer of carrots. Perhaps that is an appropriate international division of labor. Since the U.S. is going to be tougher on Iran, let the Europeans use the American bogey in place of their own stick. And since the Europeans and Japanese are going to be easier on Iran, let the Americans use them in place of their own carrot. To shift analogies, we seem to have a classic good cop / bad cop routine, in which the Europeans and Japanese are the good cop and the U.S. is the bad cop. The bad cop threatens the criminal and hits him a few times, then the good cop comes along to offer sympathy and to suggest cooperation in order to keep the bad cop from starting up again.

Such a carrot-and-stick policy has a definite appeal. It allows flexibility through adjustment of the goalposts as the situation changes. It permits half steps by each side, rather than requiring an all-or-nothing approach. It provides the public with an easily explainable framework for what could otherwise be seen as inconsistencies or as cynical realpolitik.

However, a carrot-and-stick policy has some definite drawbacks:

- The carrots may not be sweet enough. The West is unlikely to be in a position to offer Iran inducement sufficient to achieve Iran's economic aims. Even were the West to press full steam ahead with normalization of economic ties with Iran, that would still not reverse Iran's serious economic problems outlined above. Iran cannot in a short time reverse the halving of its per capita income that followed

the Revolution, especially when it pursues misguided policies of pouring billions into state-sponsored heavy industry. The amount of resources Iran would need, especially if it continues its economically inappropriate policies of extensive regulation, would be vast. Europe and Japan provided Iran with \$30 billion in loans from 1989 through 1992, with little result in terms of political moderation or economic performance (indeed, Iran had to reschedule \$11 billion falling due in 1993-94). There is no possibility that the U.S. public would tolerate, or the U.S. business community be interested in, any transfer of public or private resources on that scale.

- Economic carrots may not satiate Iran's appetite. Tehran's aims may well be grander than simple prosperity, in which case a stronger Iran be more, not less, of a problem. It is difficult to imagine the current Iranian leadership being content with only greater wealth -- they want to dominate the Gulf and to be the leading force among the world's Muslims. It is by no means clear that these goals are acceptable to the West, especially if dominating the Gulf means de facto setting oil policy for the region or if being the leader of the world's Muslims means implementing in all Muslim lands the same disregard for human rights that characterizes Iran.
- It may be hard to decide when to give Iran carrots and when to apply the stick. Consider the American hostages in Lebanon. For several years, U.S. policy was to bargain, until Washington decided Tegrans was manipulating their interlocutors by telling them what they want to hear (e.g., hostages will be released) while simultaneously acting in exactly the opposite way disguised with a moderately credible deniability (e.g., surrogates taking new hostages). U.S. diplomats argue that in the end, Tehran arranged the hostages' release precisely because the U.S. showed it would not bargain, and so that therefore the hostages brought Iran no advantage and cost it heavily (cf. *Washington Post*, January 20, 1992). In short, the stick worked. On the other hand, Tehran argues that the proffered carrot is what secured the release of the hostages. It cites President Bush's comment in his inaugural address that Iran should realize "good will begets good will." Iran's Foreign Minister Velayati has complained, "Really, the United States hasn't done anything in response to what we did in the past concerning the release of their hostages." (*New York Times*, April 14, 1992)
- Threats to apply sticks against Iran may not impress Tehran, which sees that the U.S. tolerates the continued rule of a government against which it had sent into battle 500,000 troops, i.e., Saddam Hussein. In other words, U.S. credibility may be low, especially so long as the U.S. refuses to take actions that would cost U.S. firms lost markets in Iran.

Classic Containment

The phrase "dual containment" for current U.S. policy towards Iran and Iraq was designed to emphasize that the U.S. would not seek a special relationship with either as a means to preserve a balance of power in the Gulf, and that instead the U.S. would use its own military presence to limit both. The use of the term containment to describe current U.S. policy towards Iran is misleading if it brings to mind the policy George Kennan proposed vis-a-vis the Soviet Union: lay down clear markers to avoid military confrontation, demonstrate a willingness to use force if those markers are crossed, and wait until internal problems eventually cause the regime to implode. In fact, the U.S. shrinks from this kind of containment.

Precisely because the Islamic Republic is in poor political, social, and economic shape, there is reason for optimism about a policy of containment in the classic sense. Economic weaknesses increase the chances containment would succeed, as does as the growing disillusionment of the Iranian people with rampant corruption and continuing poverty. Hashemi Rafsanjani was quite right when he warned shortly after becoming Iran's President (*Jomhuri Islami*, December 10, 1989), "Do you think the people who have no medicine and no school, we can tell them we had a revolution and keep them busy with slogans?"

Economics is not the only reason why the Islamic Republic is profoundly unpopular at home. It has exacerbated social tensions, with the six million Afghans and Sunnis bitterly detesting Persian Shia chauvinism. It has alienated many of the devout and the senior clergy, who resent political interference in religious affairs. It has made a mess of the economy, with per capita income about half of the pre-revolutionary level. Tehran's rulers feel so nervous that three times in a year (November 1994, August 1994, and December 1993), they mobilized 200,000 troops to practice protecting public buildings against rioting mobs.

The reservoir of support for the clerics, fed by the waters of hatred for the Shah, have run dry. Many remember the Shah's with nostalgia as a time of riches and social freedom, while those of prime rioting age are too young to remember him. It is quite possible that the Islamic Revolution will not last into a second generation. European experts on Iran are pessimistic about its prospects. The respected Paris newspaper *Le Monde* asked (December 24, 1994) if the Tehran regime was entering its last months. The Islamic Republic survives simply because there is no credible alternative. Like the Shah's regime, it could collapse quickly if any such alternative emerged. Unfortunately, it could also survive another decade or more if there is no good alternative.

A classic containment policy would be a much more assertive containment policy than the U.S. has at the moment. For instance, it would involve an end to statements like that of Assistant Secretary Pelletreau, who told Congress, "We believe the Iranian regime is a permanent feature." (*Washington Times*, October 20, 1994) A vigorous and strict containment policy would see the U.S. saying instead that we accept the right of the Iranian people to a government of their own choosing and we look forward to their exercising that choice more freely under a government that respects human rights.

Classic containment as practiced towards the Soviet Union did not involve much in the way of economic sanctions. There was broad Western agreement in principle on no dual use exports, as is there is towards Iran now. Indeed, the Western powers are stricter in their enforcement of that policy vis-a-vis Iran than they ever were with respect to Moscow. During the Cold War, there was no Western agreement on a policy the U.S. fitfully suggested, i.e., to deprive the Soviet Union of foreign exchange where possible and sell them all the consumer goods they wanted. European and Japanese policymakers never accepted the logic of depriving Moscow of foreign exchange. If that is what is meant by economic containment, then it was never the agreed multilateral Western policy towards the USSR.

It is interesting that the standard being demanded for economic containment of Iran is more demanding than what was applied towards Moscow. The prospects for a coordinated Western economic isolation of Iran are poor. It may be possible to isolate Iran from international capital markets because of Iran's deteriorating creditworthiness. But trade containment will be more difficult. Recent U.S. measures to curtail oil development in Iran may help. It appears such measures had as their "goal to give the Secretary of State the credibility he needs to look other members of the G-7 in the eye and say, Stop it." And they may have that effect: British Prime Minister John Major was described by the *Washington Post* (April 5, 1995) as being "in lockstep" with President Clinton in "backing increased economic pressure on Iran."

Destabilization

In November 1994, an Israeli official told a group in Washington that the West should adopt a policy to replace the Islamic republic which he said has become a "malignant tumor" in the region (*Iran Brief*, December 5, 1994). This view is what some have attributed to Speaker Gingrich.

It is difficult to see how the West could have much effect on who rules in Tehran. The U.S. does not have a major influence on Iranian domestic policy. Just as the U.S. cannot expect to shore up moderates, neither can it expect to bring about the Islamic Republic's downfall.

The People's Mojahedeen like to portray themselves as a serious threat to Tehran's continued rule. That may or may not be the case -- I find it extremely unlikely. But the Mojahedeen are almost certainly correct when they say that the key factor determining whether or not they succeed will be their own actions, not the Western support. Indeed, the Mojahedeen's foreign spokesman Mohammed Mohadession says as a matter of principle that they would refuse any aid from the U.S. were it to be offered them (personal interview, March 1995).

The other major powers do not and will not support any policy that openly and directly works to destabilize the Islamic Republic. Indeed, it is not apparent that the European and Japanese governments would act much differently from their present course if the U.S. were to adopt a policy of refusing to work with the Islamic Republic and publicly calling for its replacement with another type of government.

The Effects of Unilateral Comprehensive U.S. Sanctions on Iran

The effects of comprehensive sanctions on Iran would obviously much greater if all major industrial nations joined in. The chances that will happen are low indeed. Iran has not exposed in the kind of open outlaw behavior that Saddam exhibited in invading Kuwait or Qaddafi in organizing the downing of Pan Am 103. It is therefore unlikely that those most interested in markets and less aware of their responsibilities for world order -- and I think of the newly industrialized nations of East Asia -- will join in sanctions on Iran. Furthermore, at least some in Russia feel that a strategic relationship with Iran is in Moscow's interests, which will undermine support there for sanctions.

Any evaluation of whether the U.S. should proceed with comprehensive sanctions should therefore be based on what would happen if the U.S. acts alone.

How Sanctions Will Cost Iran Money

Comprehensive U.S. sanctions on Iran will reduce Iran's foreign exchange receipts several ways:

- Oil trade. Iran sells about one-fourth of its exported oil to U.S.-owned firms. Iran will have to sell this oil to other oil companies. Iran will have no difficulty finding other buyers for the oil. But the loss of access to U.S. firms will have a price for Iran. U.S. firms are prepared to offer slightly better terms than firms from other countries, which is exactly the reason why Iran has been selling to the U.S. companies. Now that it can no longer sell to the U.S. firms, Iran will lose that extra margin. How much money are we talking about? We will never know. The price of oil goes up or down in a month by as much as a dollar per barrel, while the sanctions price differential would probably be a few pennies on the barrel. I would be surprised if the loss were as large as five cents per barrel, or \$50 million a year.
- Planned oil swaps involving Iran and former Soviet states. The U.S.-led consortiums producing oil in Kazakhstan and Azerbaijan are planning to ship oil to Iran across the Caspian Sea. Iran would use that oil in its northern cities, especially Tehran, while increasing the export of Iranian oil from the Gulf. This swap arrangement, which could start in a matter of months, is supposed to be temporary. But we all know that nothing lasts as long as a temporary deal. Iran will earn several tens of millions of dollars a year in profits and cost-savings from this deal.
- Oil field renovation and expansion. Iran's oil fields are old; production will decline unless Iran develops more difficult to reach offshore areas and/or uses sophisticated techniques to recover more oil from aging fields. Iran has found that U.S. firms offer good terms for oil equipment, as testified by Iran's recent

preference for using the U.S. firm Conoco over the French firm Total for developing the fields off Sirri Island.

- Investor confidence. Comprehensive U.S. sanctions will add to the impression that Iran is a politically risky place to do business. European investors and bankers are already hesitant about Iran because of its heavy indebtedness, and Iranian businessmen are worried about increasing government restrictions. It is possible that comprehensive U.S. sanctions will trigger a further run on the Iranian currency, which has already lost a third of its value in 1995.

In short, sanctions could cost Iran tens of millions, if not a hundred million or more dollars, a year in export revenues and in capital invested in the country.

Comprehensive U.S. Sanctions and the Islamic Republic's Behavior

Comprehensive U.S. sanctions will reduce Iran's income by several tens of millions of dollars each year. The Iranian budget is already under tight constraints. Given the difficulties of making adjustments elsewhere, spending on the military could well go down if the sanctions are vigorously implemented.

Indeed, one of the unsung accomplishments of the current U.S. policy towards Iran is its success in forcing Iran to curtail its ambitious 1989 plan for acquiring a large-scale modern military. Iran planned to buy \$10 billion in arms in 1989-94, primarily from the Soviet Union. The arms purchases had to be cut in half when Iran was locked out of world capital markets, thanks both to its own stupid economic practices and to the U.S. pressure not to make politically-motivated loans to Iran. The difference in military potential is highly significant. Today, Iran is a threat in certain areas, mostly terrorism and weapons of mass destruction. Had Iran carried out its 1989 plan, it would be a significant conventional force that could slow or impede U.S. actions in the Gulf.

While comprehensive U.S. sanctions may reduce Iranian military spending some, there is no prospect that the Islamic Republic will fall because of sanctions. The fate of the Islamic Republic will be decided largely by internal factors. The U.S. does not have a major influence on Iranian domestic policy. Just as the U.S. cannot expect to shore up moderates, neither can we expect to bring about the Islamic Republic's downfall.

Effects of Sanctions on the U.S.

Some argue that the U.S. should woo Iran because it is the strategic prize in the Persian Gulf region. This view is outdated: Iran is no longer a country with a key economic and geostrategic position.

Iran is not an oil superpower. Its oil fields are old, and its reserves are expensive to develop. Iran produces today less oil than it did in 1970, while production has soared in other

parts of the world. In 1970, Iran produced almost 9 percent of the world's oil; today, it produces only about 5 percent. And Iran has to invest several billion dollars a year just to maintain its present output.

Iran is not a lucrative market. Iran's imports in 1994 were little more than \$12 billion, which was less than it imported in 1977. Iran's imports in 1994 were less than one-half of one percent of world imports, whereas in 1977, its imports were 1.5 percent of the world total. The simple fact is that Iran's economic importance has faded along with its oil wealth.

Conclusions

U.S. policy towards Iran is often misperceived as being tougher than it is and the difference with Japan and Western Europe as being greater than they are. Washington's aim is to modify Iran's behavior with sticks and carrots. That is very close to the policy of Japan and Western European nations, which is to modify Iran's behavior with carrots and sticks. The U.S., like its allies, wants dialogue with Iran. The U.S. does not ship to Iran much in the way of arms and dual-use technologies, including nuclear power technology; nor do Japan and Western Europe. The only major difference is on loans to Iran and imports from Iran, which Washington discourages and bans respectively, while Japan and Western Europe allow.

Were the United States to shift to a policy of containment in the sense that George Kennan used the word -- preventing external aggression while awaiting the collapse of an unworkable system -- the prospects for success are good in the long term but uncertain at best in the short term. A containment policy would succeed not primarily from any economic restrictions on Iran, but because of the shortcomings of the Iranian system of government. Western allies would probably not change their policies much if the U.S. were to adopt this policy.

Comprehensive U.S. sanctions may encourage more allied restrictions on Iran by demonstrating how seriously Washington takes the issue. But the prospects are uncertain, even if the U.S. adopts policies designed to penalize those who undermine the sanctions.

At the same time, Iran has extensive access to Russian arms and nuclear technology, a situation that is unlikely to change irrespective of U.S. policy.

As a result, the case for sanctions should not rise or fall on any prospective reaction of other countries. If applied unilaterally, comprehensive U.S. sanctions will cost Iran some tens of millions of dollars at a time when Tehran is short on funds. That could well reduce the resources Iran has to spend on its military.

The principal reason that unilateral U.S. sanctions against Iran appear attractive is the singular failure of efforts to promote moderation, efforts that included shipping arms only five years after the humiliating embassy hostage takeover. The bitter lesson of the last 15 years is that the U.S. cannot expect moderation in Iranian foreign policy if it extends a hand of friendship.



U.S. Policy toward Iran: Will Sanctions Hit Their Mark?

May 2, 1995

Statement by John H. Lichtblau, Chairman

Before the

Subcommittee on International Economic Policy and Trade
Committee on International Relations, U.S. House of Representatives

at its hearing on
U.S. Sanctions Policy on Iran: Can We Be More Effective?

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Introduction

Thank you for inviting me to testify today on U.S. sanctions policy on Iran. My testimony will discuss:

- the impact of current and proposed legislation and Executive Orders on (1) Iranian oil exports and (2) investments in the Iranian oil sector,
- S. 630, which would deny access to the U.S. market to any foreign companies dealing with Iran.
- a hypothetical analysis of the impact on the world market of a successful policy to block Iranian oil exports, and
- the impact of a ban on U.S. company purchases of Iranian oil.

Before starting our analysis I would like to state that we concur with the basic policy intent of H.R. 1033, namely, to penalize Iran for its documented continued support of international terrorist activities and its demonstrated consistent record of violations of human rights. We also recognize that economic considerations are not always the paramount consideration in our foreign policy. Any negative impact on the U.S. or its businesses, however, should be acknowledged and weighed by the policy makers.

Impact of H.R. 1033 on Iran: Minimal

Our first point, the impact of H.R. 1033 on the Iranian oil industry, has two aspects: U.S. investments in Iranian oil operations and U.S. purchases of Iranian oil.

Investment Restrictions: Non-U.S. Companies Will Step In

The investment restrictions in the bill, as spelled out in Section 3 (b) (4), have largely been addressed in Executive Order 12957, dated March 15, 1995, which prohibits all forms of U.S. investments in Iran. Issued one day before the Senate Banking Committee hearings on H.R. 1033's twin, S. 277, the Executive Order reflects a newly galvanized and articulated Administration policy, prodded by the Congressional focus on Iran and the proposed billion dollar Conoco oil field development contract with the National Iranian Oil Company. As we know, the contract, accepted and announced in Teheran, was cancelled by Conoco just before the Executive Order was issued by the President.

In the long term, the readiness of non-U.S. companies to invest will become clear. Because foreign companies do not bring to the table Conoco's unique interest in Iranian gas from the Sirri offshore field that can be piped to Dubai to facilitate the company's production there, the Conoco deal, *per se*, is not a matter of a simple transfer from one potential contractor to another. At least two European companies, however, have been reported as negotiating for the play.

Altogether, then, the Congressional initiatives on policy toward Iran, the public attention on the Conoco deal and the related White House Executive Order can be assumed to have some limited negative impact on the Iranian oil sector, both in delaying any non-U.S. contracts and in making the terms less attractive for Iran than the cancelled Conoco contract with its special attractions. The negative impact, however, will be fleeting.

Geologically and economically, Iran is one of the world's most attractive oil investment areas. Iran's current productive capacity (and actual production) is 3.6-3.7 million B/D. In the five years prior to the Iranian revolution in 1979 (and then followed by the Iran-Iraq war of 1980-89), Iran's production averaged 5.5 million B/D. The production decline is not due to a declining resource base but to a combination of neglect, war damage and lack of funds to rebuild its capacity.

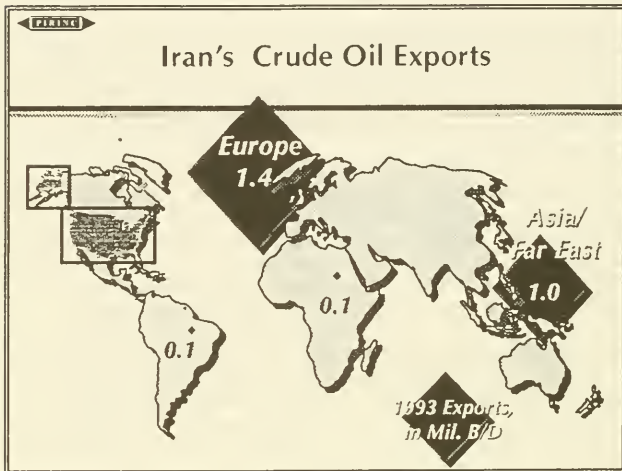
Since virtually all forecasts agree that all Persian Gulf producers must increase their output substantially between now and 2000 and again to 2010 to meet world demand, foreign investment in the Iranian oil sector should be both attractive and necessary. In the absence of U.S. companies, European oil companies can be expected to undertake these investments, regardless of U.S. policy. In the long run the blocking of U.S. investments in Iran will only hurt American companies, not Iran.

Ban on U.S. Companies' Lifting Iranian Oil: Non-U.S. Companies Will Buy It

My next point is the proposed total ban in H.R. 1033 on all Iranian oil lifting by U.S. companies and their foreign affiliates. As you know, of course, since 1987 this ban has only applied to shipments to the U.S. In testimony before the Senate Banking Committee on March 16th on this issue, we made the point that Iran's revenues will be unchanged by a lifting ban such as that in S. 277 because "unilateral embargoes don't reduce exports." Because we discussed this issue in some detail in our March 16th testimony, there have been no changes in the S. 277/H.R. 1033 since then and no new information has come to our attention, we would like to submit an abbreviated version of this section of our March 16 Senate testimony.

Iran exports about 2.6 million barrels per day of oil. As shown in the following figure, Europe takes more than half of the total, with the largest volumes moving to

France, Italy and the Netherlands. These countries together account for about 45% Europe's 1993 Iranian volumes. About 1 million B/D went to Asia and the East in 1993, with Japan accounting for 35-40% of the total. Small amounts of Iranian oil also went to Canada, Latin America, Africa, and the Mideast. At 1994 prices, the value of Iranian oil exports was approximately \$13 billion.



Some 600-650 thousand barrels per day of these exports, worth \$3.5 - 4.0 billion, were purchased by a number of U.S. companies for refining, resale or trading outside the U.S.

There have been frequent references to the large sums of money paid by U.S. oil companies to Iran, presumably strengthening the existing regime. There is no doubt that if Iran lost 600 thousand barrels per day of exports its economy would be weakened. However, the implied assumption that if U.S. companies could no longer purchase these volumes (as would be the case under H.R. 1033), Iran's oil export volume and value would decline substantially, is not borne out by the facts, in our view.

The reason is the same that caused Iran very little harm following the reinstatement of the U.S. import embargo in October 1987: no other country joined the U.S. embargo and a *unilateral trade embargo of a globally traded fungible commodity is by definition ineffective*. The U.S. Administration at the time was fully aware of this. Then-Energy Secretary John Herrington was reported to say that the embargo would have little practical effect on stemming Iran's crude oil exports unless there

was large-scale cooperation from other countries. As we know, there was none. There is currently no indication that any oil importing country has any intention to change its position on Iranian oil imports.

Thus, while passage of H.R. 1033 might cause a very short term dislocation for the 25% of Iran's oil exports bought by U.S. companies, the world oil market would quickly redistribute Iranian oil to other markets and/or customers and restore any temporary imbalances. The fact that both Iranian Light and Iranian Heavy crude are mainstream crudes that most refiners can readily process is also a positive factor in redistributing the U.S. companies' share of Iranian exports. If the National Iranian Oil Company cannot find new outlets at suitable prices immediately, it can temporarily put more oil into its storage tanks, a routine procedure in the world oil market.

S. 630: The Cost is Too High

Unacceptable to our Friends

Senator Alfonse D'Amato has recognized the possibility that foreign companies may offset any negative impact on Iran of a global embargo on Iranian oil purchases by U.S. companies and has therefore introduced S. 630. In the Senator's words, "a foreign corporation or person will have to choose between trade with the United States or trade with Iran." S. 630 goes far beyond preventing foreign companies from buying the Iranian oil that U.S. companies would be forced to leave behind under S. 277. It would force foreign companies or individuals who want to do business with the U.S. to cease buying *any* oil or other commodity from Iran. The same would apply to exports to Iran.

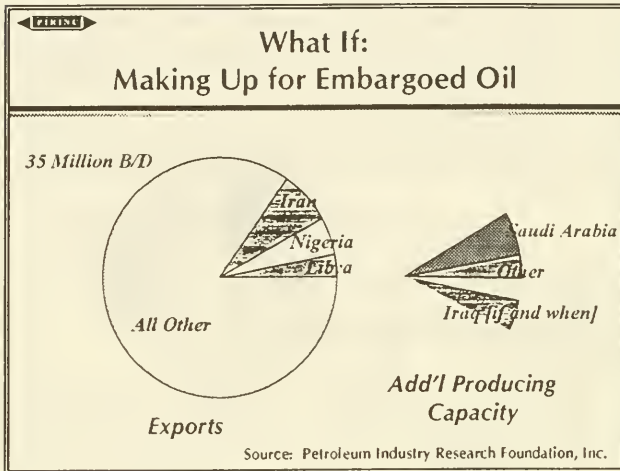
There is virtually no chance that the U.S.'s foreign trading partners would accept this form of secondary trade boycott. They could be expected to protest and then retaliate.

What If the Boycott Works?

But should we even want to see all or most Iranian oil exports eliminated? From an economic point of view, the answer is clearly *no* under current conditions. Iran is exporting about 2.6 million B/D, equal to 7.5% of total world oil exports. If all or most of these exports become unavailable, the price of oil would rise substantially because the world market would have insufficient supplies at current prices.

As shown below, the world's current excess producing capacity amounts to about 3 million B/D, of which 2 million B/D is located in Saudi Arabia. Suppose our policy succeeds in reducing Iranian oil exports by 50% or 1.3 million B/D. Under current

conditions, i.e. continuing full U.N. sanctions on Iraqi oil exports, this would reduce available world oil exports by nearly 4% and result in a price increase of perhaps \$4/Bbl. or the equivalent of 10¢/gallon in product prices



The increase would be substantially lower if Saudi Arabia and the other OPEC countries with spare capacity were to raise their production to offset the loss of Iranian exports. But how likely is such a response? It would clearly be a hostile act towards an OPEC member which actively participates in setting OPEC price and production policy. Since the reduction in Iranian exports would not be based on an official U.N. policy, as the Iraqi sanctions are, OPEC countries with spare capacity would have no reason to cooperate in a policy to hurt one of their members. Obviously, if U.S. policy should succeed in cutting Iranian exports even more than 50%, the price impact would be larger, probably on a disproportionate scale.

The problem compounds as other exporters are targeted. For instance, calls for universal sanctions against purchasing Libyan oil, if implemented, would likewise result in a oil price increase.

Thus, the advocates of imposing global restrictions on oil imports from Iran beyond the elimination of U.S. companies as purchasers of Iranian oil, are faced with a Catch-22 situation. The more they succeed in their endeavor to cut Iranian exports, the more the price of oil will rise with attendant negative impacts on the economies of all importing countries. For the moment, this is the reality of the oil market and, hence, can not be passed over.

Impact on U.S. Companies

Finally, let us examine what the proposed embargo would do to U.S. companies currently engaged in Iranian oil trade. In the broadest sense, it would be a mirror image of the bill's impact on Iran. The affected U.S. companies would have to switch to non-Iranian supply sources for the approximately 600 thousand barrels per day lifted from Iran last year. Over time, they would be able to do so. Since most of their Iranian oil transactions are under term contracts, they would probably have to declare *force majeure* to break their contractual obligations unless the legislation contains a 90-day phase-out period. The phase-out period would also smooth the impact of the embargo on the world oil market.

The U.S. oil companies, however, would not be indifferent to being denied all commercial access to Iran, currently the world's second largest oil exporter (after Saudi Arabia), while their foreign competitors maintain unrestricted access. U.S. oil companies are already handicapped *vis-a-vis* their foreign competitors by the standing, exclusively U.S., prohibition on all trade with Libya, the principal oil supplier in the Mediterranean basin. If Iran were to be added to this restriction, it would further reduce the U.S. companies' international logistical flexibility, would at times prevent them from making optimal trading and transportation arrangements, limit their ability to engage in crude price arbitrage transactions, etc.

All of this would put U.S. firms at some unquantifiable but, at times, significant disadvantage with respect to their non-U.S. competitors. In other words, U.S. companies are likely to be more affected by H.R. 1033 than its intended target, the Iranian economy.

Conclusion

As I said at the beginning of my testimony, there may well be overriding non-economic reasons for the U.S. to prohibit U.S. companies from doing business with Iran. However, as long as other countries do not actively support our policy, the impact of H.R. 1033 on the Iranian economy will be marginal, at best, and short-lived. As I pointed out earlier, while Executive Order 12957, which prohibits U.S. investment in Iran, may have had a negative impact on the Iranian oil sector, that impact is temporary and fleeting. Any dislocations of Iranian volumes from world markets as a result of a ban on U.S. company liftings of Iranian oil would likewise be fleeting. Economically, these sanctions will not hit their mark.

Question:

Now, if that estimate (when Iran could obtain a nuclear weapon) is still accurate in the range of eight years away from having that capability, what about the cost? Do we have any sense of how much of their GNP they have to divert, what kind of dollar costs that program would have?

Answer:

An historical review of the efforts of proliferators indicates that these states have followed a number of different routes in their drive to develop a nuclear weapons capability. Several variables influence the costs, which have differed widely, and make it difficult to offer a meaningful assessment of the final economic expenditure involved in these efforts.

We strongly object to any expenditure by Iran on its nuclear weapons program. We regularly urge other governments not to extend official credits or development assistance to Iran because the provision of such resources allows Tehran to divert scarce funds to its military programs.

The President's recent decision to sever the remaining trade and investment links between the United States and Iran was based, in part, upon his concern about Iran's continued pursuit of weapons of mass destruction. We will continue to spearhead the international effort to deny Iran any technology, materials, or resources that could contribute to its nuclear weapons program.

Date of Hearing May 2, 1995
Page 48
Line 1109

Question:

Is this administration operating under the assumption that the Iranians have been counterfeiting American currency?

Answer:

The USG is aware of unconfirmed reports that the government of Iran is involved in counterfeiting U.S. currency. To date, there is still no reliable intelligence to substantiate these reports. The Secret Service is the lead agency on this issue and continues to investigate as leads arise, in cooperation with the Department of State and the intelligence community.

Date of Hearing May 2, 1995
Page 52
Line 1204

Question:

Assuming that our allies do not join us in this embargo, are there any examples that you can give us where unilateral action by this country against other countries which were carrying on activities that we frowned upon actually worked?

Answer:

Unilateral U.S. embargoes do have an impact; they demonstrate our seriousness of purpose, mark the depth of our objection to a country's behavior, and set a standard for the rest of the world to match. Previous embargoes have been profoundly troubling to target countries, as they have posed a strong challenge to the legitimacy of objectionable policies and practices.

Embargoes, like all forms of political, economic, or military pressure, are most effective when multilateral. Our policy of pressuring Iran to change its unacceptable behavior has long recognized the need for international cooperation. We have achieved some important successes with other countries in restraining the export to Iran of weapons of mass destruction and their delivery systems, armaments, and sensitive dual-use technology. The United States led this critical effort by unilaterally imposing the industrialized world's strictest controls on the export of such items to Iran.

The President's recent decision to sever the remaining economic and investment links between the U.S. and Iran underscores America's readiness to lead by example. By sending an unambiguous message about the importance we attach to these interests, the President's action will strengthen our hand as we again urge other nations to adopt our approach toward Iran.

THE PRESIDENT'S EXPORT COUNCIL
WASHINGTON, D.C. 20520

April 27, 1995

The Honorable William J. Clinton
President of the United States
The White House
1600 Pennsylvania Avenue, N.W.
Washington, DC 20500

Dear Mr. President:

I understand that you are considering an Executive Order to impose further sanctions against Iran -- in part, responding to legislation now under consideration in the House and Senate. While the entire Council has not addressed this subject, Michael Jordan's subcommittee has reviewed it and I strongly share their view that broad based unilateral sanctions will carry an enormous cost to longer-term U.S. competitiveness.

We support any potentially effective action you may take that is targeted directly at state supported terrorism and proliferation of weapons of mass destruction. Such actions have a good chance of gaining multilateral cooperation and, as such, will not be harmful to U.S. international competitiveness.

I urge you not to take actions which we know will be ineffective and will hurt the United States more than the target government.

Sincerely,



C. Michael Armstrong
Chairman

cc: Secretary Christopher
Secretary Ronald H. Brown
The Honorable William A. Reinsch
The Honorable Jeffrey Garten
Members of PECSEA
The President's Export Council
Jane Siegel



The Constitutionalist Movement of Iran

STATEMENT OF THE CONSTITUTIONALIST MOVEMENT OF IRAN
IN SUPPORT OF IMPOSITION OF A TOTAL TRADE EMBARGO
(EXCEPT FOR HUMANITARIAN PROVISIONS)
ON THE ISLAMIC REPUBLIC OF IRAN

May 2, 1995

SUBMITTED TO THE COMMITTEE ON INTERNATIONAL RELATIONS OF
THE UNITED STATES HOUSE OF REPRESENTATIVES

The Constitutionalist Movement of Iran (CMI)

P.O. Box 39068 Washington, D.C. 20016 Tel: (301) 365-7277 Fax: (301) 365-4151



The Constitutionalist Movement of Iran

NOW COMES The Constitutionalist Movement of Iran ¹ and in furtherance of President Clinton's announced plan to cut off all United States trade and investment with Iran², and in support (with humanitarian exceptions) of a total imposition of an international trade embargo on the Islamic Republic of Iran proposed by Senator Alfonse D'Amato (Republican, N.Y.) and Congressman Peter King (Republican, N.Y.)³ states as follows.

BACKGROUND

On or about August 1978, a religious fanatic by the name of Ruhollah Khomeini, commenced the masterminding of a series of unthinkable terrorist activities in Iran and elimination of human rights of the Iranian people.

One of the most notable, inhumane terrorist act which was masterminded under the leadership of Ruhollah Khomeini during that period resulted in the total annihilation of more

¹ A short description of the Constitutionalist Movement of Iran and its aspirations is attached hereto as *Exhibit A*.

² See N.Y. TIMES, May 1, 1995, § A, at 1.

³ See WALL STREET JOURNAL, May 1, 1995, §A at 3.

than 250 civilians by setting a theater in Abadan (a southern portal city in Iran) on fire and locking all entrances and exits of the theater⁴. (Khomeini naturally blamed Savak, Iran's intelligence gathering organization under the former regime of Iran.⁵)

While Ruhollah Khomeini, privately, was planning acts of terror similar to the one described above, with an aim to destabilize the government of Iran; publicly, he claimed that he intended to establish a totally free and democratic society in Iran with all the safeguards inherent to a democratic regime such as freedom of the press and assembly, free elections, equality, liberty and equal justice for all⁶. To the total detriment of the Iranian people, Khomeini's duplicitous strategy outlined above (secret and underground strategy of destabilization of the government of Iran by terror and public promise of freedom and liberty) was successful in folding the last legitimate government of Iran under the last Iranian prime minister of the former regime, Shahpour Bakhtiar, in February, 1979.

Upon his arrival to Iran, Ruhollah Khomeini, together with his cohorts, contrary to all of his promises, commenced a systematic eradication of all elements of a democratic society by imposition of a state of terror in Iran the likes of which is not witnessed in modern times. Ruhollah Khomeini believed and stated publicly that those that had in any shape or form any leadership position in the society (whether political or economic) during the late Shah are guilty of transgression against God, do not need to be tried before a tribunal, and shall be summarily executed.⁷ Moreover, Ruhollah Khomeini decreed that the assets of all the said people shall be seized, liquidated, and deposited in Ruhollah Khomeini's account.⁸ The net effect of Ruhollah Khomeini's acts of terrorism against the state and people of Iran was that:

⁴ See the confessions of perpetrators of the arson of Cinema Rex of Abadan in SAMIY, AHMAD, RISE AND FALL OF THE PROVISIONAL GOVERNMENT OF IRAN n.7 at 129 (1992). See also ETELAAT, Aug. 27, 1981 (Newspaper).

⁵ *Id.*

⁶ Khomeini's duplicitous pronouncement from Neufles le Chateau, Paris in 1978.

⁷ Samiy, *supra* p. 81.

⁸ *Id.* at 53.

1. A legitimate and benevolent government was forced to collapse by acts of terrorism which were committed against people and was cleverly blamed on the so-called secret police of the state (e.g. the incident of Cinema Rex of Abadan, Iran).

2. Terrorists, under the leadership of Ruhollah Khomeini, came into possession of at least Thirteen Billion Dollars (\$13,000,000,000.00) in cash reserves and an almost endless stream of income from the oil revenue of Iran.

3. By systematically eliminating the leadership of Iran in 1979 and thereafter, under the charge of transgression against God, and confiscation of the assets of the people so accused, Ruhollah Khomeini, by terrorizing private citizens eliminated any meaningful political opposition and came into possession of billions of assets from private funds.⁹

4. With public funds in billions of dollars and with confiscated private funds of the same range, Ruhollah Khomeini commenced the so-called Islamic Fundamentalism.

THE NATIONAL SECURITY OF THE UNITED STATES DICTATES IMPOSITION OF A TOTAL TRADE EMBARGO (EXCEPT FOR HUMANITARIAN PROVISIONS) ON ISLAMIC REPUBLIC OF IRAN

The announcement by President Clinton earlier this week to end all trade by United States companies with the Islamic Republic of Iran is a welcome, progressive step in the direction of combatting world-wide terrorism, which is emanated and financed by the Islamic Republic of Iran. While the actions announced by President Clinton are to be commended,

⁹ See WALL STREET JOURNAL, May 5, 1992 for the article about the genesis of assets of the Foundation Of The Oppressed and other similarly formed foundations in Iran with assets of Eleven Billion Dollars (\$11,000,000,000.00) for the Foundation Of The Oppressed.

the United States needs to take additional measures to expunge the evil acts emanated by the Islamic Regime of Iran.

ISLAMIC REGIME OF IRAN IS NOT A LEGITIMATE GOVERNMENT AND IS A GANG OF THUGS CONTROLLING THE NATION OF IRAN

First and foremost, we have to realize that the so-called Islamic Regime of Iran is not a legitimate government in a traditional meaning of the term. The Islamic Regime of Iran does not have any characteristics of a modern government and is not even similar to a totalitarian government. The Islamic Regime indeed is a gang of thugs that came to power by terrorizing a nation and confiscating its public and private assets. The notion of people and Iranian nation does not have any meaning to these thugs. These thugs are quite similar in their behavior to a drug cartel or an oversized and giant version of a Los Angeles gang. One can become a member of this gang by manifesting a severe psychological disorder exemplified by an animalistic ability to kill, maim, terrorize, and annihilate human beings with no remorse.¹⁰ There is no evidence of a fair judiciary system in this regime which even minimally adheres to some international norm of adjudication.¹¹ There is no evidence that the government protects the assets of the people and entities that it is supposed to protect.¹² There is no evidence that the Islamic Republic of Iran protects the right of individuals that governments are ordinarily charged to protect.¹³

¹⁰ E.g. Examine the background of the leaders of these thugs, such as Khalkhali (the so-called killing judge), Mohammadi Gilani, and Lajevardi (the famous torturer).

¹¹ See generally American International Group v. Islamic Republic of Iran, 493 F.Supp. (D.C. Cir. 1980).

¹² See generally Stromberg-Carlson Corp. v. Bank Melli Iran, 467 F.Supp. 530 (S.D.N.Y. 1979); Chicago Bridge & Iron v. The Islamic Republic of Iran, 506 F.Supp. 981, (N.D. Ill. 1980).

¹³ See generally Berkowitz, et al. v. The Islamic Republic of Iran, 735 F.2d 329 (9th Cir. 1984).

However, there is ample evidence that the thugs that call themselves the Islamic Republic of Iran are in the business of hostage taking, terror, murdering innocent people, and assassinations.¹⁴ In short, the thugs who have terrorized the nation of Iran is no government.

THE THUGS OF ISLAMIC REPUBLIC OF IRAN ARE IN PURSUIT OF NUCLEAR ARMS TO FURTHER TERRORIZE THE GLOBAL VILLAGE

The thugs who call themselves the Islamic Republic of Iran, following the mastermind plan of the founder of heir cult, Ruhollah Khomeini, intend to:

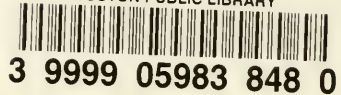
1. In public, present themselves as a legitimate political power under the guise of Islam (the so-called Islamic Fundamentalism) and duplicitously proclaim beliefs in such notions as justice for all (and especially for the poor and the oppressed who are willing to terrorize innocent human beings), equality for all (except for women who are an underclass and subservient to men), economic equality for all (which in reality is a cover for confiscation of assets of the wealthy people and nations, and nationalization of all assets for the use and enjoyment of their thugs).

2. In private, seeking all instruments for mass terror, exploring all venues for destabilizing legitimate governments, opposing all peace treaties and processes by sabotage or otherwise, and purposefully creating a chaotic system internally and globally.

In order to achieve their goals, after failing to achieve the same with conventional armament (e.g. Khomeini's failure in the war with Iraq) is to secure nuclear armament. There is ample evidence that the Islamic Republic desire to have massive nuclear energy capability is not driven by energy needs of the nation of Iran.¹⁵ Accordingly, the only

¹⁴ E.g. The hostage taking of U.S. Diplomats (1979); the bombing of the U.S. Embassy in Beirut (1983); the bombing of U.S. Marine Corps. barracks in Beirut (12983); the bombing of the Israel Embassy in Buenos Aires (1992); the explosion of the World Trade Center in New York (1993), the assassinations of Tabatabai in Washington (1980), Shafiqh in Paris (1981), and Oveissi in Paris (1984).

¹⁵ N.Y. TIMES, May 1, 1995, §A at 1.



reasonable conclusion is that the thugs of the Islamic Republic intend to use the venue of procurement of nuclear energy production for their ultimate goal of obtaining nuclear armament solely for the purpose of terrorizing our global village. Secretary Christopher states that "in terms of its organizations, programs, procurement, and covert activities, Iran is pursuing the classic route to nuclear weapons which has been followed by almost all states that have recently sought a nuclear capability".¹⁶ One might argue that the nation of Iran, if lead by a legitimate and democratically elected government, might need nuclear armament for possible defensive reasons, but to allow thugs to possess nuclear arms for the purpose of terror and violence is totally irresponsible.

TRADE EMBARGO TO STOP THE REIGN OF TERROR
BY THE THUGS OF ISLAMIC REPUBLIC

Short of a costly and politically unfeasible military intervention, the only available venue to stop the Islamic Republic from obtaining nuclear armament and further terrorizing the nation of Iran and other inhabitants of the global village is the imposition of a total trade embargo (except for humanitarian provisions) on the Islamic Republic of Iran.

If the Islamic Republic of Iran is left with access to international exchange, which she presently enjoys (approximately \$15 billion dollars annually), eventually, the Islamic Republic of Iran will procure means of production and delivery of nuclear arms. We have recently witnessed how difficult it has been to convince some of the United States' allies, such as the former Soviet Union, not to sell centrifugal machines (believed capable of production of heavy water) to Iran. It is quite possible that the Chinese, Indians, North Koreans and even Pakistanis will allow the Islamic Republic to purchase nuclear armaments in exchange for oil or hard currency.

National Security interest of the United States and the free world dictate that the Islamic Republic of Iran shall not be given an opportunity to obtain nuclear armaments; which in essence means that Iran's access to hard currency shall be eliminated, which means that a total trade embargo needs to be imposed on the Islamic Republic of Iran.

¹⁶ N.Y. TIMES, May 2, 1995, §A at 6.

**HUMANITARIAN EXCEPTIONS TO IMPOSITION OF A TOTAL TRADE
EMBARGO ON ISLAMIC REPUBLIC OF IRAN**

The Constitutionalist Movement of Iran believes that, for humanitarian purposes, certain exceptions against a total economic embargo shall be considered. These humanitarian exceptions shall include but not be limited to humanitarian donations of food and medicine, banking transactions between Iran and other nations, means of communications, whether electronic or otherwise, and post, telephone, telegraph, or telefax.

CONCLUSION

For the reasons stated above the Constitutionalist Movement of Iran respectfully submits to this honorable body that the imposition of a total trade embargo on the Islamic Republic of Iran with humanitarian exceptions is in the best security interest of the entire world.

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